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No. 86-_____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

A & E SUPPLY COMPANY, INC.,
Petitioner,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,
Respondent.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Fourth Circuit

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THOMAS R. SCOTT, JR.
E.K. STREET
STREET, STREET, STREET, SCOTT & BOWMAN
P.O. Box 2100
Grundy, VA 24614
(703) 935-2128
Attorneys for Petitioner

Of Counsel:
STEPHEN A. SALTZBURG
Professor of Law
University of Virginia
School of Law
Charlottesville, VA 22901

PRESS OF RAM PRINTING, BYATTSVILLE, MD 20781 (301) 864-6662

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QUESTIONS PRESENTED

1. Did the Court of Appeals misapply this Court's decision in *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967), in the instant case, where petitioner won a jury verdict in a diversity action in the district court and the trial judge denied respondent's motions for judgment n.o.v. and a new trial, by ordering judgment for respondent without affording petitioner a new trial on a cause of action which the trial court stated had been mistakenly taken away from the jury?

2. Did the court of appeals deny petitioner its right to a jury trial in the instant case, where the trial judge concluded at the end of trial that a cause of action had been mistakenly taken away from the jury, by ordering judgment for respondent rather than remanding the case to the trial court?

3. Did the court of appeals violate the *Erie* doctrine developed by this Court by refusing to give petitioner a new trial following an ambiguity in the jury verdict for petitioner when the governing state law clearly provided that the verdict winner should have the opportunity for clarification?

PARTIES BELOW

The following entities were parties to the proceeding in the United States Court of Appeals for the Fourth Circuit, the court whose judgment is sought to be reviewed:

A & E Supply Company, Inc.
Nationwide Mutual Fire Insurance Company

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OPINION BELOW

The district court's opinion holding that respondent waived its arson defense to the contract claim is reported at 589 F.Supp. 428 (W.D. Va. 1984). The district court's opinion denying respondent's post-trial motions for judgment n.o.v. and a new trial is reported at 612 F.Supp. 760 (W.D. Va. 1985). The court of appeals' opinion reversing the district court's entry of judgment on the punitive damage verdict and denying petitioner punitive damages is reported at 798 F.2d 669 (4th Cir. 1986) and is reproduced herein at Appendix 1a.

JURISDICTION

The judgment sought to be reviewed by writ of certiorari was dated and entered August 15, 1986. The court of appeals' order denying petitioner's request for rehearing and rehearing *en banc* was entered and filed September 26, 1986 and is reproduced herein at Appendix 20a. The statutory provision conferring jurisdiction on this Court to review the judgment in question by writ of certiorari is 28 U.S.C. § 1254(1) (1982).

FEDERAL RULES INVOLVED

Rule 50. Motion for a Directed Verdict and for Judgment Notwithstanding the Verdict

(d) Same: Denial of Motion. If the motion for judgment notwithstanding the verdict is denied, the party who prevailed on that motion may, as appellee, assert grounds entitling him to a new trial in the event the appellate court concludes that the trial court erred in denying the motion for judgment notwithstanding the verdict. If the appellate court reverses the judgment, nothing in this rule precludes it from determining that the appellee is entitled to a new trial, or from directing the trial court to determine whether a new trial shall be granted.

STATEMENT OF CASE

A & E Supply Co., Inc., petitioner herein, filed suit in the Circuit Court for Buchanan County, Virginia, alleging that respondent, its insurer, wilfully and in bad faith refused to honor its fire loss claim following a fire totally destroying petitioner's warehouse and inventory. Respondent removed the action to the United States Dis-

trict Court for the Western District of Virginia.[1] Petitioner filed an amended complaint prior to trial alleging, *inter alia*, breach of contract, conversion, fraud, slander, bad faith dishonor of a first-party insurance obligation, and violation of the Virginia Unfair Insurance Practices Act, 6A Va. Code § 38.1-49, *et seq.*

The case was tried before a jury after the trial court held that respondent had waived any arson defense to the contract claim by its inconsistent payment to a "co-loss payee" in contrast to its refusal to pay petitioner.[2] Petitioner conclusively established that respondent never intended to honor the contractual claim even though it had no reasonable ground to decline payment. Petitioner also proved that respondent sent letters to its bank and various suppliers falsely accusing petitioner of arson with the intent to pressure it into settling the claim for less than the policy limits.

At the close of petitioner's evidence and again at the close of all the evidence, respondent moved for a directed verdict. The trial judge denied respondent's motions and submitted the case to the jury after first directing a verdict for petitioner on the stipulated value of the warehouse. The trial judge instructed the jury that if petitioner "is entitled to be compensated for its damages,"

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[1] As the Court will see, the fact that the action was removed effectively determined the outcome of the case. The court of appeals refused to follow state law preserving a verdict winner's right to a new trial when an appellate court finds an ambiguity in a jury verdict. The result reached by the court of appeals could not have occurred had this case remained in state court.

[2] This was a state law issue, and the trial court's ruling, reported at 598 F.Supp. 428 (W. D. Va. 1984), was never challenged by respondent.

then the jury "may also" award punitive damages. The jury returned the directed verdict for the structural coverage and a general verdict for the maximum inventory coverage under the policy totaling approximately $221,000.00. The jury also returned a special verdict awarding $500,000.00 in punitive damages finding that respondent acted in bad faith by committing the torts alleged and that the effect of respondent's conduct was to drive petitioner out of business.

Respondent then moved for judgment n.o.v. or, alternatively, for a new trial. The trial judge denied both motions in his memorandum opinion carefully reviewing all of the evidence and the uncontroverted facts supporting the jury verdict. 612 F.Supp. 760 (W.D. Va. 1985).[3] The trial court entered judgment on the verdict finding that petitioner proved respondent acted in bad faith[4] and converted petitioner's business records to prevent it from garnering the necessary evidence to successfully litigate the disputed value of its inventory claim.

The trial court further concluded in its post-trial memorandum that

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[3] The trial court granted respondent's motion for judgment n.o.v. on the fraud count because petitioner failed to prove it by clear and convincing evidence. The trial court also found that respondent violated the Virginia Unfair Insurance Practices Act, 6A Va. Code § 38.1-49, *et seq.*, but conditionally awarded petitioner a new trial because it erroneously excluded evidence of repetitive violations required by the statute.

[4] The trial court stated that "[i]f there has ever been a case in which the facts justify a finding of bad faith by an insurance company adjusting a fire loss, this is the case. The evidence is almost undisputed that [respondent] acted in bad faith in handling [petitioner's] claim." 612 F. Supp. at 772.

> [a]mong the separate, independent, wilfull torts pled by [petitioner] in the amended complaint was the tort of slander. The court denied the motion to allow the allegation of slander because it was not mentioned in the original suit. Slander was proven by strong evidence [under general allegations of bad faith] and the court is now of the opinion that error was committed by not permitting [petitioner] to amend its complaint in view of the change made by the *Kamlar* decision.[5] There was undisputed evidence that [respondent] told creditors that [petitioner] had deliberately burned its building to collect on the insurance policy. It was further shown that this slander was damaging to [petitioner], preventing the commencement of any new business and severely limiting its ability to obtain credit.

612 F.Supp at 762, n.1.

The trial court had no occasion to embody these findings in a directed verdict for petitioner because it sustained the jury verdict awarding everything requested in the amended complaint and entered judgment on the verdict. But, the trial court's opinion is clear that it viewed these matters as undisputed.

Respondent appealed, claiming that its motion for judgment n.o.v. should have been granted. The court of appeals held as a matter of first impression that the Virginia Supreme Court would not recognize the tort of bad

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[5] *Kamlar* referred to the Virginia Supreme Court's decision in *Kamlar Corp.* v. *Haley*, 224 Va. 699, 299 S.E.2d 514 (1983), which was decided after petitioner's suit was originally filed. The Virginia Supreme Court held in *Kamlar* that punitive damages may be recovered for breach of contract where the breach amounts to an independent, wilful tort. 224 Va. at 705, citing *Wright* v. *Everett*, 197 Va. 608, 615, 90 S.E.2d 855, 860 (1956).

faith dishonor of a first-party insurance obligation.[6] 798 F.2d at 676-678. Although the court of appeals found that petitioner proved conversion of its business records, 798 F.2d at 673, it reversed the punitive damage verdict, holding that petitioner failed to prove compensatory damages for conversion in addition to those underlying the contract claim.[7] *Id.*

Petitioner then filed a petition for rehearing and rehearing *en banc* pointing out (1) that the trial court instructed the jury that it must find petitioner established its right to compensatory damages before awarding punitive damages; (2) that state law guaranteed that a verdict winner would not be deprived of its judgment as a result of an ambiguity in a jury verdict;[8] (3) that respond-

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[6] The court of appeals also held that the Virginia Supreme Court would not recognize an implied private cause of action under the state's Unfair Insurance Practices Act, 6A Va. Code § 38.1-49, *et seq.*, and that the punitive damage verdict could not stand on this ground. Since both predictions involve pure questions of state law, petitioner does not challenge either holding for purposes of this petition for certiorari. Petitioner also does not challenge the court of appeals' holding that it failed to prove fraud by clear and convincing evidence under state law.

[7] The court of appeals further commented that conversion was not factually bound to the contract breach, 798 F.2d at 673. Respondent never raised this contention on appeal or during the proceedings before the trial court.

[8] Petitioner also pointed out that the Virginia Supreme Court would soon decide whether compensatory tort damages must be proved in addition to those in an interrelated contract breach to sustain a punitive damage award. *See Jefferson Coals, Inc.* v. *Eagle Energy, Inc.*, Record No. 860031 (appeal awarded July 28, 1986). Petitioner included a copy of the appeal certificate in the addendum to its petition and urged the court of appeals to remand the case to the trial court to allow the parties to avail themselves, if necessary, of the Virginia Supreme Court's binding interpretation of state law on this question.

ent never contended on appeal or during the proceedings before the trial court that conversion was not factually bound to the contract breach;[9] and (4) that the trial court had no opportunity to address the independent tort of slander which does not require proof of compensatory damages to support a punitive damage verdict.[10] Petitioner specifically cited both state law and this Court's decision in *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967), in support of its contention that it would be an extreme injustice to deny it a jury trial on the slander claim and an opportunity to clarify the verdict finding conversion. The court of appeals denied rehearing without explanation or opinion.

REASONS FOR GRANTING THE WRIT

This is not a case involving a jury award of excessive damages[11] or a trial court's grant of judgment n.o.v. following a jury verdict in favor of a plaintiff. On the con-

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[9] Had respondent raised this contention at trial, petitioner would have asked the trial court to submit to the jury, as part of the special verdict, the question whether conversion was committed in aid of the contract breach. The court of appeals denied petitioner any opportunity to have this factual issue considered by the trial court or a jury. In any event, punitive damages were recoverable if petitioner proved compensatory or nominal damages for conversion regardless of whether conversion was actually bound to the breach.

[10] Virginia law does not require proof of compensatory damages to support a punitive damage verdict for slander. *See Newspaper Publishing Corp.* v. *Burke*, 216 Va. 800, 805, 224 S.E.2d 132, 136 (1976). The district court was deprived of any opportunity to even consider the cause of action for slander because the court of appeals declined to remand the case for further proceedings.

[11] At no point during the appeal did respondent claim that the jury verdict was excessive. Its sole claim was that punitive damages could not be recovered in any amount.

trary, this case presents a setting in which the parties tried their case before a jury that found for petitioner, and in which the trial court summarized in a carefully detailed post-trial opinion the reasons why the jury verdict was not only proper but also inevitable. The court of appeals did not find a single error in the trial court's recitation of the facts or its conclusion that respondent's bad faith had been proved by uncontradicted evidence. 798 F.2d at 670.

The court of appeals did not disturb the trial court's decision upholding the jury verdict on the tort of conversion. Instead, it declared that petitioner failed to prove compensatory damages in connection with the tort of conversion and, therefore, could not recover punitive damages. Despite the fact that the trial judge expressly declared that he erred in denying petitioner the right to proceed on its slander claim and the fact that respondent did not challenge this declaration, the court of appeals disregarded the slander cause of action entirely. As a result, petitioner has never had an opportunity to have either the trial court or a jury pass on the merits of its slander claim.

As explained below, petitioner submits that the decision by the court of appeals ignores the teaching of this Court in *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967), because it deprived petitioner—the verdict winner—of a claim that the trial court specifically found had merit after conducting the trial on other claims. As a result of the court of appeals' ruling, petitioner was denied the right to trial by jury guaranteed by the Seventh Amendment.

The court of appeals' decision further denied petitioner its right to a new trial following an ambiguous verdict, despite state law holding that a verdict winner in the same

position should not be denied recovery simply because a verdict is not as clear as an appellate court would like. Without citing any authority for using its own standard rather than state law, the court of appeals implicitly followed prior decisions in the circuit holding that a federal court should apply federal law in every diversity setting when deciding whether to take a case from a jury. Petitioner submits that the court of appeals' approach is overbroad and incorrect under the *Erie* doctrine, and that it is inconsistent with the holdings of this Court and those of at least two other circuits. By granting review, this Court can clarify a serious conflict among the circuits as to the relationship of federal and state law with respect to the burden of persuasion.

A. The Court Of Appeals Misapplied This Court's Decision In *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967), By Ordering Judgment For Respondent Without Affording Petitioner a New Trial On A Cause Of Action Which The Trial Court Stated Had Been Mistakenly Taken Away From The Jury.

In *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967), this Court examined the factual setting in which a verdict winner loses on appeal but may have an additional ground to support his claim that has not been litigated. The plaintiff in *Neely* successfully litigated a wrongful death action in the district court, where the defendant's motions for a directed verdict and judgment n.o.v. were denied. On appeal, the defendant prevailed. This Court stated that under these circumstances a plaintiff with an additional meritorious claim should have an opportunity to raise it. The Court cited Fed. R. Civ. P. 50(d) and stated that the verdict winner may raise the claim in his petition for rehearing or petition for certiorari. 386 U.S. at 329-330.

In the instant case, petitioner advised the court of appeals in its petition for rehearing that its cause of action for slander had not been litigated. Petitioner cited authority clearly indicating that compensatory damages need not be proved under state law to support a punitive damage verdict.[12] Thus, petitioner complied with the procedure established by this Court in *Neely*, but the court of appeals both misapplied and ignored it. *See also*, *Weade* v. *Dichmann, Wright & Pugh, Inc.*, 337 U.S. 801, 808-809 & n.8 (1949).

This Court has not had the occasion to revisit *Neely* in almost twenty years. Although the plaintiff in *Neely* did not assert a claim either on rehearing or certiorari suggesting a new trial ground, petitioner has done so both in the court of appeals and again in this Court. The trial court recognized its error in dismissing the slander claim, but had no way of correcting it since petitioner prevailed on the jury verdict in any event. Only when the court of appeals overturned the trial court's judgment did the slander claim become crucial. When the court of appeals declined to remand this claim, it denied petitioner any opportunity to have it addressed at all and left petitioner remediless. Petitioner finds itself in the anomalous position of possessing a viable claim declared meritorious by the trial court, but which it cannot have decided on the merits. This dilemma is exactly what *Neely* intended to avoid.

B. The Court Of Appeals' Refusal To Remand The Slander Claim For Consideration On The Merits Denied Petitioner Its Seventh Amendment Right To Trial By Jury.

Ordinarily, a litigant whose claim is dismissed by a trial court may appeal to the court of appeals and seek reversal

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[12] See, e.g., Zayre, Inc. v. *Gowdy*, 207 Va. 47, 147 S.E.2d 710 (1966); *Newspaper Publishing Corp.* v. *Burke*, 216 Va. at 805, 224 S.E.2d at 136.

of the dismissal order. An exception arises, however, when the litigant has other claims that remain in the trial court and fully prevails on them. This Court has established that a successful litigant may not appeal or cross-appeal from a decision awarding everything sought in the lower court. *See New York Telephone* v. *Maltbie*, 291 U.S. 645, 646 (1934). Thus, even had the trial court failed to recognize its error in refusing to permit amendment of the complaint to include the slander claim, petitioner could not have appealed that ruling to the court of appeals. The fact that the trial court recognized its error in its post-trial opinion did not give petitioner a right of appeal, a point the court of appeals apparently overlooked. 798 F.2d at 671.

When the court of appeals reversed the punitive damage verdict and refused to remand the case for further proceedings in the trial court, it effectively deprived petitioner of the opportunity for a jury trial on the slander claim. This result deprived petitioner of its right to trial by jury guaranteed by the Seventh Amendment. The deprivation is substantial and especially unfortunate in view of the trial court's post-trial opinion clearly stating that the slander claim is extremely meritorious.

The court of appeals' approach disregards the importance of a litigant's right to a jury trial on the merits of a claim. As this Court stated in *Cone* v. *West Virginia Pulp & Paper Co.*, 330 U.S. 212 (1947), "a litigant should not have his right to a new trial foreclosed without having had the benefit of the trial court's judgment on the question." *Id.* at 217. In the instant case, the trial court's judgment was made known—i.e., that petitioner's slander claim was meritorious. But, the court of appeals effectively directed a verdict on the claim without having been asked to do so and in the face of petitioner's specific request for remand

so that its claim could be decided on the merits.[13] Petitioner asks this Court to hold that a court of appeals may not deny a verdict winner's right to trial by jury on the merits of a claim that the trial court did not find it necessary to reach.

C. The Court Of Appeals Violated The *Erie* Doctrine As Developed By This Court When It Refused To Give Petitioner A New Trial That Would Have Been Given Under State Law Following An Ambiguity In A Jury Verdict.

The record in this case conclusively establishes that the trial court, presided over by a Virginia judge applying Virginia law, instructed the jury, with respect to the tort claims on which punitive damages were sought, that if petitioner "is entitled to be compensated for its damages," then the jury "may also" award punitive damages. The trial court's reference to "its damages" obviously refers to compensatory damages on the tort claims since it held prior to trial that respondent waived any arson defense to the contract claim and directed the jury to return a verdict on the stipulated value of petitioner's warehouse. Thus, the jury had to find that petitioner proved entitlement to compensatory damages for conversion before it could award punitive damages. But, the court of appeals, applying Virginia law as no state court ever had previously or has since, held that petitioner had not adequately proved compensatory damages for conversion to support the punitive damage verdict.

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[13] *Cone* prohibited a court of appeals from entering judgment in favor of a party who had not moved for judgment n.o.v. in the trial court. The court of appeals effectively accomplished in the instant case what this Court prohibited in *Cone*. *See also, Globe Liquor Co.* v. *San Roman*, 332 U.S. 571 (1947).

Both petitioner and the trial court relied upon the logical and reasonable proposition that as long as the jury found that actual damages were proved it could award punitive damages for conversion.[14] This was and is Virginia law, and the instruction that the trial court gave was similar to the one that had just been approved four years earlier by the Virginia Supreme Court.[15]

The court of appeals apparently found that petitioner could not recover punitive damages in federal court because it only asked the jury to find, rather than to award, compensatory damages arising from the conversion.[16] This additional requirement—that compensatory damages be awarded—was not required by state law; state law required only that the jury find actual damages before awarding punitive damages. Under this Court's decision in *Erie Railroad Co.* v. *Tompkins*, 304 U.S. 64 (1938), and its progeny, the court of appeals had no basis for insisting upon more specific findings with respect to compensatory damages than a state court would have required.

If, however, there was any ambiguity in the jury verdict with respect to the finding of actual damages, state law

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[14] *See generally, Peacock Buick, Inc.* v. *Durkin*, 221 Va. 1133, 1137, 277 S.E.2d 225, 227 & n.3 (1981), which approved a jury instruction in a conversion case that permitted a verdict for punitive damages only upon a finding of actual damages.

[15] *See Peacock Buick, Inc., supra*, note 15.

[16] The court of appeals may have assumed that the jury's failure to award compensatory damages on the conversion claim meant that petitioner had not proved to the jury's satisfaction compensatory or even nominal damages on that claim. Any such assumption is not in accord with the trial court's instruction or this Court's holding in *Iacurci* v. *Lummus*, 387 U.S. 86 (1967), and at least warrants remand for clarification of any ambiguity in the jury verdict.

requires that the verdict winner be given the opportunity for further proceedings. In *Zedd* v. *Jenkins*, 194 Va. 704, 74 S.E.2d 791 (1953), the plaintiff successfully litigated a claim for alienation of affection and criminal conversion, but the jury returned a verdict for punitive damages only. The Viginia Supreme Court held that the plaintiff was entitled under those circumstances to have the case remanded for a determination of whether compensatory or nominal damages supported the punitive damage award. In *Zedd*, the Virginia Supreme Court was concerned that the verdict "was illegal in that it contained an assessment of punitive damages without finding that plaintiff was entitled to any compensatory, or even nominal, damages." 194 Va. at 708.

Zedd is important for two reasons: First, it established more than thirty years before the instant case was decided that a plaintiff who obtains a punitive damage award is entitled to that award without any specific award for compensatory damages; even a finding of nominal damages is sufficient. Second, *Zedd* established that if there is any doubt about whether the jury found nominal or actual damages, the plaintiff is entitled to a remand for further proceedings.

The court of appeals ignored *Zedd* and rejected petitioner's request for remand.[17] Apparently, the court of

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[17] The remand would have afforded the trial court, which instructed the jury on the law and conducted the instructions conference with the parties' counsel, an opportunity to determine that there was no ambiguity and that the jury had, in fact, found actual damages. In light of the trial court's findings of undisputed fact, it might even have directed a verdict that compensatory or nominal damages had been proved. Alternatively, the trial court might have conducted a new trial limited to the question whether there were actual or nominal damages as a result of conversion.

appeals believed that it had authority to enter final judgment under Fed. R. Civ. P. 50 notwithstanding *Zedd*. The court of appeals' approach to federal—state relations is consistent with a line of cases it has decided beginning with *Davis Frozen Foods, Inc.* v. *Norfolk Southern Rwy.*, 204 F.2d 839, 842 (4th Cir. 1953). These cases hold that federal law determines whether a diversity claim should be taken from the jury and decided by the court. *Wratchford* v. *S. J. Groves & Sons, Co.*, 405 F.2d 1061 (4th Cir. 1969) and continues with the decision in the instant case.

Petitioner submits that the court of appeals approach is inconsistent with this Court's decisions in *Cities Service Oil Co.* v. *Dunlap*, 308 U.S. 208 (1939), *Palmer* v. *Hoffman*, 318 U.S. 109 (1943), *Guaranty Trust Co.* v. *York*, 326 U.S. 99 (1945), and *Byrd* v. *Blue Ridge Rural Electric Corp.*, 356 U.S. 525 (1958). These cases either expressly or impliedly stand for the proposition that a federal court of appeals may not change the elements that a plaintiff must prove on a state law claim in a diversity case. This authority establishes that a federal court may not deny a plaintiff the chance guaranteed by state law to correct any ambiguity in a verdict. The court of appeals' approach is also in conflict with the decisions of the Seventh Circuit in *Lykos* v. *American Home Insurance Co.*, 609 F.2d 314 (7th Cir. 1979) and *McMahon* v. *Eli Lilly & Co.*, 774 F.2d 830 (7th Cir. 1985), and the decision of the Eighth Circuit in *Crossman* v. *Trans World Airlines*, 777 F.2d 1271 (8th Cir. 1985). These cases hold that a federal court must follow state law in deciding whether to take an issue away from a jury.

Petitioner further submits that the court of appeals misapplied this Court's decision in *Hanna* v. *Plumer*, 380 U.S. 460 (1965). There is nothing in the Federal Rules of Civil Procedure that suggests, let alone requires, that a

litigant be denied a remand for clarification of a verdict. The court of appeals' approach finds no support in Fed. R. Civ. P. 50(d) and is inconsistent with this Court's interpretation of Rule 50(d) in *Neely, supra*. This Court in *Neely* provided a mechanism for the court of appeals to do exactly what the Virginia Supreme Court would have done in the instant case.[18] When the court of appeals departed from the requirements of state law, it created both an unnecessary and undesirable conflict between federal and state law.

The court of appeals' approach is also inconsistent with the First Circuit's in *Marshall* v. *Mulrenin*, 508 F.2d 39 (1st Cir. 1974). The First Circuit held in *Marshall* that this Court's decision in *Hanna* does not require application of the federal rules of procedure in such a rigid fashion that would impair a substantive state interest. In short, the court of appeals created a substantial conflict in federal—state relations in the instant case without there being any apparent tension between Fed. R. Civ. P. 50 and Virginia law.

Had the instant case been tried in the state trial court where it was originally filed, petitioner would not have been denied an opportunity to clarify the jury verdict. That the denial in this case resulted because the court of appeals declined to defer to established state law indi-

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[18] This Court stated in *Neely* that "where the court of appeals sets aside the jury's verdict because the evidence was insufficient to send the case to the jury, it is not so clear that the litigation should be terminated." 386 U.S. at 327. The Court further stated that where the trial court caused the insufficiency the verdict winner would be entitled to a new trial. *Id*. Thus, petitioner would be entitled to a new trial under both federal and state law.

cates an insensitivity to the principles of *Erie* and other decisions of this Court.

CONCLUSION

Petitioner submits that the issues presented in this case are of great importance, both with respect to federal procedure and federal—state relations. Petitioner respectfully asks this Court to grant the petition and to reverse the decision of the court of appeals for the reasons stated herein.

Respectfully submitted,

THOMAS R. SCOTT, JR.
EUGENE K. STREET
STREET, STREET, STREET, SCOTT
& BOWMAN
P.O. Box 2100
Grundy, VA 24614
(703) 935-2128
Attorneys for Petitioner

Of Counsel:
STEPHEN A. SALTZBURG
Professor of Law
University of Virginia
School of Law
Charlottesville, VA 22901

APPENDIX

APPENDIX
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 85-1759(L)

A & E SUPPLY COMPANY, INC.,

Appellee,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,

Appellant.

No. 85-1780

A & E SUPPLY COMPANY, INC.,

Appellant,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,

Appellee.

Appeal from the United States District Court for the Western District of Virginia, at Big Stone Gap. Glen M. Williams, District Judge. (C/A 81-0140).

Argued: February 6, 1986 Decided: August 15, 1986

Before ERVIN and WILKINSON, Circuit Judges, and HOUCK, United States District Judge for the District of South Carolina, sitting by designation.

W. Charles Waddell, III and S. D. Roberts Moore (Guy M. Harbert, III; Gentry, Locke, Rakes & Moore; Howard C. McElroy; White, Elliott & Bundy on brief) for Appellant/cross-appellee; Eugene K. Street (Thomas R. Scott, Jr.; Street, Street, Street, Scott & Bowman on brief) for Appellee/cross-appellant.

WILKINSON, Circuit Judge:

This case presents a familiar problem in insurance law. The insured sustained a financial loss for which the policy promised indemnification. The insurer denied coverage, contending without factual support that the insured was responsible for the catastrophe. In the subsequent lawsuit, the insured recovered the proceeds due and also received punitive damages, which it had sought on the theory that the insurer's breach constituted several independent, wilful torts. The insurer now appeals from this punitive, noncontractual award. We find that the insured did not prove the alleged fraud or the alleged conversion and that Virginia law would not recognize either the tort of bad faith refusal to honor a first-party insurance obligation or an implied private right of action under the state's unfair insurance practices statute. We therefore reverse that portion of the judgment awarding punitive damages.

I.

In the late evening of October 27 and the early morning of October 28, 1980, a fire completely destroyed the building of the A & E Supply Company, a mining equipment business in Buchanan County, Virginia. Owned and operated by brothers Larry Fletcher and Terry Lee Fletcher, A & E had purchased from the Nationwide Mutual Fire Insurance Company a policy that provided $150,000 in protection for the building and $250,000 in protection for its contents. A & E immediately notified Nationwide of the loss and gave to Nationwide what invoices, receipts, and tax returns had survived the fire.

Nationwide examined these documents and investigated the events of October 27-28. On March 12, 1981, Nationwide unreasonably refused to pay A & E, charging that the Fletchers had intentionally set the fire.

Nationwide did not relay its unfounded suspicions to law enforcement authorities for proper investigation, an admitted violation of the Arson Reporting Immunity Act. Va. Code § 27-85.3 *et seq.* Nationwide did, however, tell the creditors of A & E that the Fletchers had burned the building to collect on their insurance policy. These allegations severely limited the Fletchers' access to credit while Nationwide's cancellation of all A & E policies limited the Fletchers' access to insurance and Nationwide's refusal to return the A & E documents limited the Fletchers' access to information. Together the actions prevented resuscitation of the mine supply business and pressured the Fletchers to settle the A & E insurance claim quickly and unfavorably.

Instead, A & E sued Nationwide for breach of the insurance contract, conversion of the business records, acquisition of the records by false pretenses, fraud, slander, trespass, intentional infliction of emotional distress, bad faith dishonor of a first-party insurance obligation, and violation of the Virginia Unfair Insurance Practices Act, Va. Code § 38.1-49 *et seq.*[1] Because Nationwide had in May 1981 remitted $66,000 on the policy to the co-insured Borg-Warner Acceptance Corporation, the district court held that Nationwide had waived its arson defense, and the court accordingly granted a partial summary judgment of liability on the contract claim. *A & E Supply Co.* v.

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[1] Title 38.1 of the Virginia Code defined the relations of insured and insurer at the time of the coverage denial and the ensuing complaint. Virginia has since repealed title 38.1 and substituted a new insurance code in Title 38.2 of the Virginia Code, effective July 1, 1986. Under Va. Code § 1-16, this repeal does not "in any way whatever . . . affect . . . any right accrued, or claim arising before the new law takes effect." Our decision therefore addresses the rights of A & E under Title 38.1.

Nationwide Mutual Fire Insurance Co., 589 F.Supp. 428 (W.D. Va. 1984). Nationwide does not appeal from this ruling. Also before trial, the district court dismissed as improperly pleaded the A & E claims of slander, trespass, and intentional infliction of emotional distress. A & E does not appeal from those rulings.

From May 30, 1984 to June 12, 1984, a jury in the Western District of Virginia heard testimony and arguments about the compensatory damages due on the policy and about the punitive damages sought on the basis of Nationwide's conduct. The jury returned a directed verdict for $32,069.79 in coverage on the stipulated value of the building and returned a verdict for $188,966.09 in coverage on the contested value of the inventory. The jury also found in special verdicts that Nationwide had converted the business records of A & E, had obtained these records by false pretenses, had committed fraud, had acted in bad faith, and had engaged in unfair trade practices. Finding further that Nationwide had been malicious, the jury granted the request of A & E for $500,000 in punitive damages.[2]

Nationwide moved on all counts for a new trial or for judgment notwithstanding the verdict. The district court conditionally granted a new trial on the count pertaining to the state unfair trade practices act and granted judgment notwithstanding the verdict on the count alleging fraud. The court denied all of Nationwide's other motions. *A & E Supply Co.* v. *Nationwide Mutual Fire Insurance Co.*, 612 F.Supp. 760

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[2] A & E had moved under Fed.R.Civ.P. 15(a) to amend its complaint in order to ask for more punitive damages, a request that the district court denied and that A & E now pursues on appeal. We do not address this assignment of error, however, because of our conclusion that A & E was entitled to no punitive damages.

(W.D. Va. 1985).[3] Nationwide now concedes the judgment for compensatory damages, costs, and interest. It appeals from the judgment for punitive damages.

II.

Damages for breach of contract in Virginia normally "are limited to the pecuniary loss sustained." *Kamlar Corporation* v. *Haley*, 224 Va. 699, 299 S.E.2d 514, 517 (1983), *quoting Wright* v. *Everett*, 197 Va. 608, 90 S.E.2d 855, 860 (1956). The measure of damages is related to the exchange of risk and obligation in the agreement itself. The duty of each party toward the other is what that party has promised and covenanted. In a sense, each party has contracted for some outer limit to its liability.

It would skew the predictability necessary for stable contractual relations if a breaching party were suddenly subject to the more open and unanticipated duties and damages imposed by the law of tort. Most courts, and certainly Virginia courts,

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[3] At the same time, A & E had moved under Fed.R.Civ.P. 60(b)(6) for relief from the judgment preventing recovery of its attorneys' fees pursuant to Va. Code § 38.1-32.1. The court denied this petition on the reasoning that § 38.1-32.1 applied to an "individual" who is a natural person but did not extend to corporations. *A & E Supply Co.* v. *Nationwide Mutual Fire Insurance Co.*, 612 F.Supp. 760, 776-777 (W.D. Va. 1985). The Virginia General Assembly, however, has subsequently stated that "'Individual,' as used in this section, shall mean and include any person, group, business, company, organization, receiver, trustee, security, corporation, partnership, association, or governmental body, and this definition is declaratory of existing policy." Va. Code § 38.2-209. This legislative construction of Va. Code § 38.1-32.1 is entitled to significant weight in the interpretation of an ambiguous statute. *Cf. Seatrain Shipbuilding Corp.* v. *Shell Oil Co.*, 444 U.S. 572, 596 (1980). On its authority, we reverse the decision that A & E is ineligible under § 38.1-32.1 and remand to the district court for further consideration of attorneys' fees.

have thus not recognized an exception to the general rule of damages, even when the breaching party acts with an alleged malicious motive. The circumstances surrounding the dissolution of contractual relations are so frequently beset by strain and suspicion that perceptions of improper motive on the part of an opposing party are commonplace. Breach of contract would thus routinely give rise to an action in tort, with its attendant incentive of a punitive award. The Virginia Supreme Court has noted that "the overwhelming weight of authority continues to resist this tendency." *Kamlar Corp.* v. *Haley*, 299 S.E.2d at 517.

The general rule of contractual damages in Virginia admits but one exception. Only if the breach establishes the elements of "an independent, wilful tort," may it support an award of punitive damages. *Id.* In this case, the societal interest in the deterrence and punishment of wrongdoing may be implicated apart from any breach of contract. Viewed from this perspective, an "independent tort" is one that is factually bound to the contractual breach but whose legal elements are distinct from it.

A & E Supply has sought in this litigation to establish "an independent, wilful tort" on the part of Nationwide and to place itself within the exception. It argues that the jury and the district court correctly identified two such independent wilful torts—conversion and bad faith refusal to pay a first-party insurance claim—and contends that the district court erred in overturning the jury on two others—fraud and violation of the Virginia Unfair Insurance Practices Act. While we sympathize with the plight of plaintiff and agree with the district court that the conduct of Nationwide Mutual Fire Insurance Company was discreditable, we cannot find in the above litany of torts one that both applies to the circumstances of this case and that Virginia law would recognize as an independent basis for the award of punitive damages.

III.

A & E first seeks to uphold the award of punitive damages through proof of the familiar independent, wilful torts of fraud and conversion. Virginia law defines actual fraud as the knowing misrepresentation of a material fact to another person, whose reasonable reliance on the misrepresentation results in damage. *Packard Norfolk, Inc.* v. *Miller*, 198 Va. 557, 95 S.E.2d 207, 210 (1956). "The general rule is that fraud must relate to a present or a pre-existing fact, and cannot ordinarily be predicated on unfulfilled promises or statements as to future events." *Soble* v. *Herman*, 175 Va. 489, 9 S.E.2d 459, 464 (1940). A plaintiff may recover for actual fraud by showing reasonable reliance on a promise made by a defendant who had no intention of performing, *Colonial Ford Truck Sales, Inc.* v. *Schneider*, 228 Va. 671, 325 S.E.2d 91 (1985), but the plaintiff must prove all of the elements of fraud by clear and convincing evidence, *Martin* v. *Williams*, 194 Va. 437, 73 S.E.2d 355, 359 (1952).

That evidence is absent here. A & E argues that Nationwide's agent made fraudulent misrepresentations immediately after the fire to Larry Fletcher that "I think we can help you" and that Nationwide might "possibly" pay quickly on the claim. A & E also says that it entrusted its records to Nationwide in the belief that "as quick as they can get these records estabished, that they would have a settlement, or a partial settlement for us to where we could get back in business quickly." But such tentative statements to Larry Fletcher, made soon after the fire had ended and the investigation had begun, were more perfunctory reassurances than promises of payment. As the district court noted, A & E could not reasonably have relied on a belief that Nationwide had at this early point made any decision on the claim. Furthermore, the delivery of the A & E documents to Nationwide was required by the insurance contract and did not demonstrate reliance on the insurer's preliminary expectations of coverage. The district

court properly concluded that the evidence failed to substantiate the allegations of fraud.

A slightly different path leads to the same conclusion about the allegations of conversion.[4] A & E did prove that Nationwide had, in withholding A & E documents, wrongfully interfered with the company's rights to its own business records. *Cf. Buckeye National Bank* v. *Huff & Cook*, 114 Va. 1, 75 S.E. 769, 772 (1912) (defining conversion as "any wrongful exercise or assumption of authority, personally or by procurement, over another's goods, depriving [the other] of their possession"). But these elements of conversion cannot alone sustain the judgment granting punitive damages. Under Virginia law, an award of compensatory damages "is an indispensable predicate for an award of punitive damages, except in actions for libel and slander." *Gasque* v. *Mooers Motor Car Co.*, 227 Va. 154, 313 S.E.2d 384, 388 (1984). *See also Peacock Buick, Inc.* v. *Durkin*, 221 Va. 1133, 277 S.E.2d 225, 227 & n.3 (1981) (approving jury instruction in conversion suit that permitted verdict for punitive damages only upon finding of actual damages). This principle required A & E to buttress its conversion case with proof that the dispossession involved a palpable loss.

Again, the necessary evidence is absent here. A & E has claimed actual damages exclusively through Nationwide's failure to pay on the insurance contract. Its damages stemmed from this breach of contract, not from the alleged tort of conversion. The allegations of conversion, furthermore, describe tortious conduct that was extraneous to the breach of contract. Nationwide did not refuse to return the A & E records until April 29, 1981, more than six weeks after Nationwide

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[4] Although the jury returned separate verdicts on conversion and on the acquisition of property by false pretenses, both parties have recognized that the tort of conversion, extending to any wrongful act of procurement, subsumes the allegations of false pretenses. We accordingly treat the two counts together and find that, for the same reason, neither theory may support an award of punitive damages.

had formally rejected the insurance claim. The wrongful retention of property was not factually bound to the breach but to the efforts of Nationwide to prove its position in the ensuing litigation. A & E did not request the return of documents until it had initiated suit. It would undermine the rule of *Kamlar Corp.* v. *Haley* if subsequent disputes over evidence were to translate into the tort of conversion sufficient to support a punitive damages award in an action for contractual breach. A & E, which recovered its documents under a pre-trial order, has not alleged or proved any other actual damages from the conversion. The award of punitive damages accordingly may not rest on the conversion count.

IV.

A & E also claimed at trial that the requisite support in tort for an award of punitive damages could be found in its right to recover from Nationwide under the Virginia Unfair Insurance Practices Act, Va. Code § 38.1-49 *et seq.* Bound by the decision in *Morgan* v. *American Family Life Assurance Co. of Columbus*, 559 F.Supp. 477 (W.D. Va. 1983), the district court held that the statute implied a private cause of action in tort for insureds against insurers who had violated the Act. The jury returned a verdict of liability, but the district court then ruled that an insured could recover only for repeated violations of the Act. Because the court had suppressed evidence of such consistent conduct, it overturned the verdict and conditionally granted a new trial on the claim of unfair practices. *A & E Supply Co.* v. *Nationwide Mutual Fire Insurance Co.*, 612 F.Supp. 760, 774-775 (W.D. Va. 1985). On appeal, we first examine the premise in *Morgan* v. *American Family Life Assurance Co.* Not obliged to follow that precedent, we conclude that the Virginia Unfair Insurance Practices Act does not establish a private cause of action. We therefore vacate the conditional order for a new trial and remand with instructions to enter judgment for Nationwide on the statutory count.

The Virginia legislature enacted its Unfair Insurance Practices Act to define all practices that constitute "unfair or decep-

tive acts or practices" and to prohibit "the trade practices so defined or determined." Va. Code § 38.1-49. The legislature based the Act on a model statute drafted by the National Association of Insurance Commissioners, an example that has been followed by many other states. *See* Comment, *Insurers and Third-Party Claimants: The Limits of Duty*, 48 U.Chi.L.Rev. 125, 146 n.75 (1981). The Act forbids various insurance practices, including failure in bad faith to settle claims for which liability is reasonably clear. *See* Va. Code § 38.1-52.9(6). To enforce these regulations, the statute delegates to the State Corporation Commission the authority to promulgate rules, to investigate insurers, to conduct hearings, and to impose sanctions. Va. Code §§ 38.1-53 to 38.1-56. The Commission, acting largely through the Insurance Commissioner, may order insurers to cease and desist from prohibited practices, may levy penalty fines, and may suspend or revoke insurance licenses. Va. Code §§ 38.1-55 to 38.1-56. The statute guarantees Supreme Court review of final Commission orders, Va. Code § 38.1-56.1, but does not expressly create or preclude a private right of action against insurers who have committed proscribed trade practices.[5]

The federal district court in *Morgan* v. *American Family Life Assurance Co.*, 559 F.Supp. at 483-85, addressed this

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[5] The Act provides at Va. Code § 38.1-57.1 that "no order of the Commission under this article shall in any way relieve or absolve any person affected by such order from any liability under any other laws of this Commonwealth." This section does not authorize the A & E lawsuit, much as Va. Code § 8.01-221 "does not create any new rights of action but instead preserves any existing right of action that an injured person may have against a wrongdoer who has previously been the subject of statutory penalties for his misconduct." *Morgan* v. *American Family Life Assurance Co. of Columbus*, 559 F.Supp. 477, 484 (W.D. Va. 1983). *See also Hortenstine* v. *Virginia-Carolina Ry. Co.*, 102 Va. 914, 47 S.E. 996 (1904). As the court in *Morgan* v. *American Family Life* observed, 559 F.Supp. at 485, neither provision answers the question of whether an implied right of action exists under the Unfair Insurance Practices Act.

silence through *Cort* v. *Ash*, 422 U.S. 66, 95 S.Ct. 2080, 45 L.Ed.2d 26 (1975). The Virginia Supreme Court has not, however, adopted the *Cort* rationale for finding an implied private right of action under federal law to the interpretation of state legislation. As a further matter, federal courts should be reluctant to read private rights of action into state laws where state courts and state legislatures have not done so. Without clear and specific evidence of legislative intent, the creation of a private right of action by a federal court abrogates both the prerogatives of the political branches and the obvious authority of states to sculpt the content of state law.

It is clear that the Virginia Supreme Court would not read the Unfair Insurance Practices Act to create a private right of action in tort. The Court has long regarded the state legislature as a repository of sovereign powers, whose dispensation must in any context be strictly construed. Describing "the doctrine of implied powers" in *Commonwealth* v. *County Board of Arlington County*, 217 Va. 558, 232 S.E.2d 30, 42 (1977), the Court said that "the rule is clear that where a power is conferred and the mode of its execution is specified, no other method may be selected; any other means would be contrary to legislative intent and, therefore, unreasonable." The Unfair Insurance Practices Act confers a power to redress insurer misconduct by organizing a system of administrative oversight with appellate judicial review. Under the approach of *Commonwealth* v. *County Board of Arlington County*, a court may not add a regime of private lawsuits to this specified mode of executing the statutory purpose. To do so would be to violate the injunction that "the doctrine of implied powers should never be applied to create a power that does not exist or to expand an existing power beyond rational limits." *Id.* 232 S.E.2d at 42.

The disinclination of the Virginia Supreme Court to recognize an entitlement that has not clearly been legislated is also supported here by a due regard for other provisions that have clearly been legislated. *Cf. National Maritime Union of Amer-*

ica v. *City of Norfolk*, 202 Va. 672, 119 S.E.2d 307, 314 (1961) ("It is an elementary rule of statutory construction that all relative provisions of a legislative enactment must be considered and read together in construing one provision or section."). The Unfair Insurance Practices Act is but one part of the state insurance code, a statutory complex that fills more than four hundred pages of the Virginia Code. The enactment provides for extensive regulation of insurance rates, availability, and practices. Tensions among these goals are to be resolved by the State Corporation Commission, which Va. Code § 38.1-29 charges "with the execution of all laws relative to insurance and insurance companies." *Blue Cross of Virginia* v. *Commonwealth ex rel. State Corporation Commission*, 218 Va. 589, 239 S.E.2d 94, 96 (1977).

The measured concord within this program would likely be disrupted by the introduction of state and federal courts as decision-makers affecting only one dimension of interrelated insurance problems. The most casual glance at the action below shows the inconsistencies that would result. The punitive damages awarded by the jury greatly exceeded the penalties provided in the Act. Va. Code §§ 38.1-55 to 38.1-56 (penalty not to exceed $5,000 per violation and $50,000 aggregate for six-month period). The requirement that frequent commissions of unfair claim settlement practices under Va. Code § 38.1-52.9 exist for a statutory violation appears more consistent with continued regulatory oversight than an individual cause of action. The discordant effects of independent—and often inexpert—supervision of unfair trade practices by the jury encourages acceptance of the explicit statutory remedy as the exclusive statutory remedy. As one commentator has advised, "if the legislature has carefully chosen an enforcement mechanism to accomplish the legislative purpose by accommodating conflicting interests, the integrity of the overall statutory scheme requires restraint in implying private actions." Note, *Implied Causes of Action in the State Courts*, 30 Stanford L.Rev. 1243, 1253 (1978).

Our reading of Virginia law accords with the position of several state courts that the model unfair practices legislation

proposed by the National Association of Insurance Commissioners, as enacted in those states, does not create a private right of action. *See, e.g., Patterson* v. *Globe American Casualty Co.*, 101 N.M. 541, 685 P.2d 396 (Ct. App. 1984); *Seeman* v. *Liberty Mutual Insurance Co.*, 322 N.W.2d 35 (Iowa 1982); *Wilder* v. *Aetna Life & Casualty Co.*, 140 Vt. 16, 433 A.2d 309 (1981); *Scroggins* v. *Allstate Insurance Co.*, 74 Ill.App.3d 1027, 30 Ill.Dec. 682, 393 N.E.2d 718 (1979); *Cohen* v. *New York Property Insurance Underwriting Association*, 65 A.D.2d 71, 410 N.Y.S.2d 597 (1978); *Russell* v. *Hartford Casualty Insurance Co.*, 548 S.W.2d 737 (Tex. Civ.App. 1977); *Retail Clerks Welfare Fund Local No. 1049, AFL-CIO* v. *Continental Casualty Co.*, 71 N.J. Super. 221, 176 A.2d 524 (1961).[6] In deferring to administrative primacy as a limitation on the adjudicative role, we also parallel interpretation of the Federal Trade Commission Act, 15 U.S.C. § 41 *et seq.*, whose basic prohibition of "unfair or deceptive acts" is tracked by the Virginia statute. Because the substantive prohibitions of that statute were "inextricably intertwined with provisions defining the powers and duties of a specialized administrative body charged with its enforcement," courts have declined to imply any private right of action and have relied upon the regulatory scheme to police the industry. *See Holloway* v. *Bristol-Myers Corporation*, 485 F.2d 986, 989 (D.C. Cir. 1973). We believe that the Virginia Supreme Court, while following its unique line of precedent and reasoning, would share many of the

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[6] To be sure, some other states have found an implied cause of action in their versions of the model act. *Klaudt* v. *Flink*, 658 P.2d 1065 (Mont. 1983); *Jenkins* v. *J. C. Penney Casualty Insurance Co.*, 280 S.E.2d 252 (W. Va. 1981); *Royal Globe Insurance Co.* v. *Superior Court of Butte County*, 23 Cal.3d 880, 153 Cal. Rptr. 842, 592 P.2d 329 (1979). We belive that the Virginia Supreme Court would either distinguish these decisions as dependent on variations from the Virginia Code, *see e.g. Royal Globe Insurance Co.* v. *Superior Court*, 592 P.2d at 333 (noting textual difference between California and Virginia statutes), or would find the other decisions to be unpersuasive.

concerns discussed by these courts and would reach the same result. We therefore hold that the award of punitive damages to the A & E Supply Co. may not rest on a jury finding that Nationwide violated the Unfair Insurance Practices Act.[7]

V.

As a final "independent, wilful tort" on which to predicate punitive damages in accordance with *Kamlar Corp.* v. *Haley*, 224 Va. 699, 299 S.E.2d 514, 517 (1983), A & E points to the verdict against Nationwide on its refusal in bad faith to honor a first-party insurance obligation.[8] In denying Nationwide's motion for judgment notwithstanding the verdict, the district court ruled that Virginia would recognize such a tort and that A & E had proved the elements. No Virginia authority directly addressed these issues; the court predicted the course of state law by reference to the Virginia Unfair Insurance Practices Act, the duty of good faith in the performance of insurance contracts, and the established right of action for refusal in bad faith to honor a third-party insurance obligation. *A & E Supply Co.* v. *Nationwide Mutual Fire Insurance Co.*, 612 F.Supp. 760, 770-772 (W.D. Va. 1985). But as we have already explained, the Unfair Insurance Practices Act does not imply the availability of any remedies beyond those described in the statute. Similarly, the extrapolation from the duty of good faith and the analogy to the third-party precedent do not support

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[7] We note that the revised Unfair Insurance Practices Act, effective July 1, 1986, provides that "No violation of this section shall of itself be deemed to create any cause of action in favor of any person other than the Commission; but nothing in this subsection shall impair the right of any person to seek redress at law or equity for any conduct for which action may be brought." Va. Code § 38.2-510(B).

[8] An insurer's first-party insurance obligation is its duty to compensate the insured for direct losses within the policy coverage. An insurer's third-party insurance obligation is its duty to defend the insured against claims by another, injured party and to indemnify the insured for losses sustained through such claims.

the district court's conclusion. To the contrary, these considerations indicate that Virginia would join the jurisdictions that have declined to recognize a remedy in tort for refusal in bad faith to honor a first-party insurance claim. We therefore reject this last basis for the award of punitive damages.

All contracting parties owe to each other a duty of good faith in the performance of the agreement. *Restatement (Second) of Contracts* § 205 (1981). For Nationwide, this duty parallels the insurer's responsibility under Va. Code § 38.1-52.9(6) to attempt "in good faith to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear." The doctrinal roots of the obligation are notoriously elusive: one scholar has argued that actions for bad faith sound in "conequitort," suggesting the interaction among concepts of contract, equity, and tort. Holmes, *Inductions from a Study of Commercial Good Faith in First-Party Insurance Contracts*, 65 Cornell L.Rev. 330, 377 (1977). This case, however, requires us to define the duty within the parameters of Virginia law, for A & E may receive punitive damages if Nationwide's conduct was tortious but may not receive punitive damages if Nationwide's conduct was "only a breach of contract inspired by an ulterior motive." *Kamlar Corp.* v. *Haley*, 299 S.E.2d at 518.

We hold that in a first-party Virginia insurance relationship, liability for bad faith conduct is a matter of contract rather than tort law. The obligation arises from the agreement and extends only to situations connected with the agreement. *Cf. Reisen* v. *Aetna Life and Casualty Co.*, 225 Va. 327, 302 S.E.2d 529, 533 (1983) ("the existence of the [good faith] duty wholly depended upon a condition precedent, that is, coverage under the policy"). The nonconsensual nature of the duty does not necessarily remove it from the province of contract; the Virginia Supreme Court has long enforced similar bonds in contract despite an absence of an express promise among the parties. *See, e.g, Carpenter* v. *Virginia-Carolina Chemical Co.*, 98 Va. 117, 35 S.E. 358 (1900). Indeed, insofar as the obligation is imposed by Va. Code § 38.1-52.9, its status as a contractual

term is a routine application of Virginia principles. "It is an elementary rule of construction of insurance contracts that such a statutory provision is as much a part of the policy as if incorporated therein." *State Farm Mutual Automobile Insurance Co.* v. *Duncan*, 203 Va. 440, 125 S.E.2d 154, 157 (1962).[9]

The state law of tort, on the other hand, cannot so easily accommodate an action for bad faith performance in insurance contracts. Because every agreement involves some variation of the duty of good faith, the remedy would quickly expand beyond its original basis. As the Supreme Court of Utah noted in *Beck* v. *Farmers Insurance Exchange*, 701 P.2d 795, 800 (Utah 1985), courts adopting the A & E reasoning "appear to have had difficulty in developing a sound rationale for limiting the tort approach to insurance contract cases." Tort relief in this situation implies tort relief in similar commercial and employment cases. *See Seamen's Direct Buying Service, Inc.* v. *Standard Oil Co.*, 36 Cal.3d 752, 206 Cal. Rptr. 354, 686 P.2d 1158, 1166-67 & n.6 (1984). Virginia law, however, explicitly forecloses that possibility. In *Kamlar Corp. v. Haley*, the Virginia Supreme Court refused "to turn every breach of contract into a tort" and held that an employee did not state a tort claim by charging that his employer "was 'actuated by malicious motives' in breaching the contract of employment." 299 S.E.2d at 517, 518. We believe that the Supreme Court would reach the analogous conclusion that an insured does not state a tort claim by charging that an insurer was actuated by bad faith in breaching the contract of insurance. *Accord, Wallace* v. *Hartford Insurance Co.*, 583 F.Supp. 1108 (W.D. Va. 1984). The better authority supports that view. *See, e.g., Beck* v. *Farmers Insurance Exchange; Spencer* v. *Aetna Life and*

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[9] An acknowledgement that the statute creates contractually enforceable duties does not conflict with a determination that the statute creates no private right of action, for contractual interpretation and statutory construction are separate enterprises. The cause of action recognized here may be in many ways different from a cause of action derived in tort from the statute.

Casualty Insurance Co., 227 Kan. 914, 611 P.2d 149 (1980); *Lawton* v. *Great Southwest Fire Insurance Co.*, 118 N.H. 607, 392 A.2d 576 (1978).

Because the suit for bad faith performance is thus in effect an action on the insurance policy, "the provisions of the contract govern the measure of recovery rather than any rules applicable to cases sounding in tort," *Bickel* v. *Nationwide Mutual Insurance Co.*, 206 Va. 419, 143 S.E.2d 903, 905 (1965). For some types of breach, these provisions might successfully limit the available damages to the stated amount of indemnity. *See* Annot., 47 A.L.R.3d 314 (1973). But if an indemnitor has violated the contractual duty of good faith, the indemnitee may recover full general and consequential damages. *See Board of Supervisors of Stafford County* v. *Safeco Insurance Co. of America*, 226 Va. 329, 310 S.E.2d 445, 450 (1983) (predicating surety's liability for consequential damages on finding of bad faith default); *see also Beck* v. *Farmers Insurance Exchange*, 701 P.2d at 801-802; *Lawton* v. *Great Southwest Fire Insurance Co.*, 392 A.2d at 579-580; *Reichert* v. *General Insurance Co.*, 59 Cal. Rptr. 724, 428 P.2d 860, 864 (1967), *vacated on other grounds*, 68 Cal.2d 822, 69 Cal.Rptr. 321, 442 P.2d 377 (1968). Had A & E proved foreseeable losses, not susceptible to mitigation, resulting from Nationwide's bad faith refusal to pay, Virginia contract law would make A & E whole. The same principles of reimbursement will not support exemplary damages, however, for such an award is designed "not so much as compensation for the plaintiff's loss as to warn others, and to punish the wrongdoer." *Wright* v. *Everett*, 197 Va. 608, 90 S.E.2d 855, 859 (1956).

Permitting consequential damages within the scope of contract law lessens the incentive for an insurer to postpone satisfaction in hopes of pressuring the insured to accept a fraction of his due. *Beck* v. *Farmers Insurance Exchange*, 701 P.2d at 798. The distress that persons experience at times of personal or financial loss leaves them vulnerable to exploitation, a temptation that would be enhanced if the insurer's contractual liability

could never, as a matter of law, extend beyond the policy limits for even the most flagrant breach. *Lawton* v. *Great Southwest Fire Insurance Company*, 392 A.2d at 579 ("The policy limits restrict the amount the insurer may have to pay in the performance of the contract, not the damages that are recoverable for its breach."). Holding that the duties and obligations of the parties are contractual does not, therefore, absolve the insurer of the need to investigate claims, to settle promptly and fairly those that are covered, and to proceed generally in good faith as that term is defined in Va. Code § 38.1-52.9.

The definition of an insurer's responsibility through consequential damages in contract rather than punitive damages in tort is also consistent with the relationship between the first-party claims of A & E and the third-party claims in *Aetna Casualty & Surety Company* v. *Price*, 206 Va. 749, 146 S.E.2d 220 (1966). In *Aetna Casualty*, the Virginia Supreme Court held that a liability insurer must answer for a judgment in excess of the promised coverage if the insurer has in bad faith refused to settle within the policy limits on a claim against its insured. This approach is grounded in contract. *See* Comment, *Insurers' Liability for Excess Judgments in Virginia: Negligence or Bad Faith?*, 15 U.Rich.L.Rev. 153 (1980). The full judgment was due the insured for foreseeable losses resulting from the insurer's breach of the duty of good faith. Although the proper range of consequential damages may vary in insurance cases, *id.* at 161-162, the guiding principle of reimbursement for provable loss appears to be settled. No Virginia authority indicates that punitive damages are available in the third-party context. *Cf. Swiatlowski* v. *State Farm Mutual Auto Insurance Co.*, 585 F.Supp. 965 (W.D. Va. 1984) (withholding judgment on issue). Even less should punitive damages be recoverable for bad faith breach in the first-party context where the insured is not "wholly dependent upon the insurer to see that, in dealing with claims by third parties, the insured's best interests are protected." *Beck* v. *Farmers Insurance Exchange*, 701 P.2d at 799. The award to A & E on this basis must accordingly be reversed.

VI.

Like the implication of a private right of action under the Unfair Insurance Practices Act, creation of a cause in tort for bad faith refusal to settle an insurance claim carries profound consequences. On the one hand, these two actions may reduce delay and obstruction in recoveries by those insured. On the other, they may deter assertion even of the most legitimate defenses by insurers. These two actions—and the large punitive awards that potentially accompany them—would portend significant changes in standards of insurer conduct and costs of insurance coverage. Whether those effects bode good or ill is not for us to say. Virginia, through its courts and legislature, is the one to restructure its insurance industry, not the federal courts through implication of private rights of action under statute and creation of venturesome torts at common law.

Here the insured sued under the policy and recovered its proceeds. The punitive award is another matter. We cannot conclude that a particular instance of conduct on the part of a particular insurer authorizes us to undertake wholesale changes in Virginia insurance law. Examination of the various foundations for the punitive verdict in the law of tort persuades us that it cannot stand. That judgment is therefore

REVERSED.

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 85-1759
No. 85-1780

A & E SUPPLY COMPANY, INC.,

Appellee,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,

Appellant.

FILED
Sep 26 1986
U.S. Court of Appeals
Fourth Circuit

Appeal from the United States District Court for the Western District of Virginia, at Big Stone Gap. Glen M. Williams, District Judge.

The appellee's petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no member of the Court requested a poll on the suggestion for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

Entered at the direction of Judge Wilkinson, with the concurrence of Judge Ervin and Judge Houck, United States District Judge, sitting by designation.

For the Court,

/s/ John M. Greacen

JOHN M. GREACEN

CLERK

86-1087

No. 86-_____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

A & E SUPPLY COMPANY, INC.,
Petitioner,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,
Respondent.

SUPPLEMENTAL APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

THOMAS R. SCOTT, JR.
E.K. STREET
STREET, STREET, STREET, SCOTT & BOWMAN
P.O. Box 2100
Grundy, VA 24614
(703) 935-2128
Attorneys for Petitioner

Of Counsel:
STEPHEN A. SALTZBURG
Professor of Law
University of Virginia
School of Law
Charlottesville, VA 22901

PRESS OF RAM PRINTING, HYATTSVILLE, MD 20781 (301) 864-6662

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A & E SUPPLY COMPANY, INC.,
Plaintiff,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,
Defendant.

Civ. A. No. 81-0140-B.

United States District Court,
W.D. Virginia,
Big Stone Gap Division.

June 15, 1984.

MEMORANDUM OPINION

GLEN M. WILLIAMS, District Judge.

The plaintiff, A & E Supply Company, Incorporated (hereinafter "A & E"), brought this action against the defendant, Nationwide Mutual Fire Insurance Company (hereinafter "Nationwide"), in the Circuit Court of Buchanan County, Virginia, alleging that Nationwide breached its insurance agreement by denying the plaintiff's fire loss and that the defendant's actions in handling the claim were malicious and wanton and violated good faith and fair dealing. The defendant petitioned the court for removal of the case pursuant to 28 U.S.C. § 1441(a). A & E is a corporation organized under the law of the Commonwealth of Virginia with its principal place of business in Buchanan County; Nationwide is incorporated under the laws of the State of Ohio with its principal place of business in Columbus, Ohio. The amount in controversy, excluding interest and costs, exceeds ten thousand dollars ($10,000). Thus, the court has jurisdiction over this suit based upon 28 U.S.C. §§ 1332 and 1441(a).

At a hearing on May 9, 1984, the court denied the plaintiff's motion for partial summary judgment and gave the plaintiff ten (10) days in which to amend its complaint to state, in separate counts, any independent torts originally alleged in the first complaint. *Kamlar Corp.* v. *Haley*, 224 Va. 699, 707 299 S.E.2d 514, 518 (1983). This case now is before the court on the plain-

tiff's motion to alter or amend the denial of summary judgment pursuant to Rule 59(e) of the Federal Rules of Civil Procedure.

I. FACTS

The relevant facts are undisputed. Nationwide issued a fire insurance policy numbered 53SM 367-494-A005 to the plaintiff on June 6, 1979. Under the policy, the building had $150,000 worth of property coverage, and the personal property had $250,000 worth of coverage. Liability coverage for bodily injury and property damage was $300,000 per occurrence. The listed mortgagee of the realty was Cumberland Bank & Trust Company in Grundy, Virginia. Effective March 7, 1980, the policy was amended so that Borg-Warner Acceptance Corporation, lienholder on the inventory, became a named loss payee. The loss payable clause stated: "Loss, if any, shall be adjusted with the Insured [A & E] and Borg-Warner Accept[ance] Corp[oration], 400 Allen Drive, P.O. Box 6731, Charleston, W. Va. 25302, as their interests may appear." This policy was in effect from April 25, 1979 to May 3, 1981.

On October 27, 1980, a fire totally destroyed the insured's building and its contents. After conducting a detailed investigation, the representatives of Nationwide concluded that the cause of the fire was arson by the two principals of the corporate plaintiff, Larry Fletcher and Terry Fletcher. Under the insurance contract Nationwide could pay the mortgagee and would be subrogated to all the rights of the bank. Consequently, the insurer paid the mortgagee. Another provision of the policy which listed the exclusions from coverage explicitly precluded insurance coverage for any criminal, fraudulent, or dishonest act that the insured or its officers instigated. On March 12, 1981, Nationwide denied liability for the plaintiff's claim because the insurer concluded the officers of A & E set the fire, and A & E began the present action about a month later. Nationwide, in its answer, raised the defenses of arson and misrepresentation as to the cause of the fire and amount and value of the personalty involved in the fire. Then in May, 1981, Nationwide paid the sum of $66,000 to Borg-

Warner, the co-loss payee, to settle its claim; Borg-Warner was to assign its security and instruments of indebtedness to Nationwide.

Based upon this payment the plaintiff filed a motion for partial summary judgment on the defendant's defenses of arson and misrepresentation, alleging that it had waived or was estopped to assert these defenses when it paid the co-loss payee. After both parties submitted memoranda to support their positions and argued the motion, the court denied the motion on the arson defense. Having reconsidered its judgment, the court vacates the previous Order denying the motion and enters partial summary judgment in favor of the plaintiff.

II. DISCUSSION

The issue presented is whether the defenses of arson and misrepresentation may be impliedly waived by paying a co-loss payee under Virginia law. The general rule is: "An insurer which, with knowledge of a breach of condition, pays the full amount of loss to the insured thereby waives the breach of condition or the right to declare a forfeiture." 44 Am.Jur.2d. *Insurance* § 1672 at 663 (1982). The Virginia Supreme Court adopted this rule in the case of *Hartford Fire Ins. Co.* v. *Mutual Savings & Loan Co.*, 193 Va. 269, 68 S.E.2d 541 (1952). The case involved an automobile insurance policy excluding coverage when the car was encumbered unless the security interest was noted in the policy. The insurance company paid a third party for the loss of the car and later contended it had no knowledge of the bank's lien. The Virginia Supreme Court held that the insurer was charged with knowledge of the lien and receipt of notice of the lien and that the insurance company waived the breach of the condition or its right to declare a forfeiture by paying the full amount to the insured.

> Where a right to rely upon a forfeiture has been once waived, it cannot be revived. *Monger* v. *Rockingham Home Mutual Fire Ins. Co.*, 96 Va. 442, 444, 31 S.E. 609. The general rule is "where an insurer, with knowledge of the breach of a condition, pays the amount of loss ascer-

> tained by appraisers into court on an interpleader, or pays or partially pays any loss under the policy, it recognizes the policy as still in existence and must be considered to have waived its defense, unless the policy is severable so that under the law it would be only forfeitable in part and the payment is made on the nonforfeitable portion." 26 C.J. *Insurance* § 1425 at 338; 45 C.J.S. *Insurance* § 743 at 754.

Id. at 276, 68 S.E.2d at 545. In reaching this conclusion the state court relied upon a Texas case, *Fidelity Lloyds of America* v. *Geddie*, 116 Tex. 656, 296 S.W. 500 (1927). The facts revealed that Geddie purchased an insurance policy protecting him against the theft of his car provided it was locked. The car was stolen while unlocked and unattended. Under a loss payable clause the insurer paid the investment company but refused to pay the balance to the insured because he forfeited the right to recover when he left the care unsecured. The Texas Supreme Court concluded that under the single, indivisible contract the insurance company waived the forfeiture by paying the investment company. *Id.* at 658, 296 S.W. at 502, *quoted in Hartford Fire Ins. Co.* v. *Mutual Savings and Loan Co.*, 193 Va. at 276-77, 68 S.E.2d at 545-46.

Only one generally accepted exception exists to this rule: "The principles of estoppel and implied waiver do not operate to extend coverage of an insurance policy after the liability has been incurred or the loss sustained." *Insurance Co. of North America* v. *Atlantic Nat'l. Ins. Co.*, 329 F.2d 769, 775 (4th Cir. 1964) (citation omitted). In that case Atlantic filed a SR21 form with the Virginia Commissioner of Motor Vehicles stating that its policy was in effect at the time of the accident. Atlantic subsequently denied liability based upon two specific exclusions: Operation of the vehicle outside of New York without written permission and liability only for bodily injury to the passenger. North American contended that Atlantic waived or was estopped to rely on these exclusions because if filed a SR21 form representing that the policy was effective on the day of the accident. The Fourth Circuit Court of Appeals concluded that the Virginia Supreme Court would hold that Atlantic would not

be estopped from relying on its policy exclusions despite the filing of the SR21 and the representations in it. *Id.* at 774. It is well-settled that "the doctrines of implied waiver and of estoppel, based upon the conduct or action of the insurer, are not available to bring within the coverage of a policy risks not covered by its terms, or risks expressly excluded therefrom, and the application of the doctrines in this respect is therefore to be distinguished from the waiver of, or estoppel to assert, grounds of forfeiture." *Id.* at 775 (citation omitted). The plaintiff is not seeking to extend the coverage of its insurance policy; thus, this one exception is inapplicable to the case at bar.

The defendant argues that the element of intention to waive is missing.

> "Waiver" is the voluntary, intentional relinquishment of a known right. Such waiver may result either from affirmative acts of the insurer or its authorized representatives, or its nonaction with knowledge of the facts. Consideration is not generally considered essential, although, if it were, it could generally be obtained from reliance by the insured upon such waiver, failure to obtain other insurance, and the like. The circumstances must indicate that the relinquishment is intended by the insurer, and the insurer must have full knowledge of all facts pertaining thereto.

16B J. Appleman, *Insurance Law & Practice* § 9081 at 489-91 (1981). *See* 44 Am.Jur.2d *Insurance* § 1572 at 581-82 (1982). While waiver is an intentional relinquishment of a known right or privilege, "it is not necessary, in order to waive a claim, that a party be certain of the correctness of the claim and of its legal efficacy; it is enough if he knows of the existence of the claim and of its reasonably possibly efficacy." 28 Am.Jur.2d *Estoppel and Waiver* § 158 at 841 (1966). Another general rule also follows that:

> In an action on a contract of insurance, the insurance company is generally considered estopped to deny liability on any matter arising out of the fraud, misconduct, or negligence of an agent of the company. So too, if either

> party must suffer from an insurance agent's mistake, it must, as a rule, be the insurance company, his principal.

44 Am.Jur.2d *Insurance* § 1612 at 616 (citation omitted). Contrary to the defendant's argument, the record reveals that Nationwide intended to pay Borg-Warner and that at the time it made the payment, it knew of the defenses of misrepresentation and arson against A & E. Robert E. Allen, Jr., a representative of Nationwide, described the mistake as follows:

> As stated in my earlier Affidavits, Nationwide's payment to Borg-Warner was a mistake. During my training as an insurance adjuster with Nationwide, I had been taught that all lienholders named on autmobile insurance policies were entitled to be paid for losses regardless of any acts or neglects of the named insureds. I did not know that named mortgagees and loss payees are accorded different protections under fire insurance policies. Because of that lack of knowledge, I recommended to my supervisor that Borg-Warner (a loss payee) and Cumberland Bank & Trust Company (a named mortgagee) both be paid their losses resulting from the Fire without regard to the policy defenses Nationwide had asserted against the plaintiff. My supervisor, Reese J. Whitley, apparently had the same understanding because he concurred with my payment recommendations. I then proceeded to pay Borg-Warner.

(Affidavit of Robert E. Allen, Jr. filed May 10, 1984 at 2). Thus, no mistake of fact existed on the part of Nationwide. The mistake arose from the agent's failure to understand the legal significance of the payment. Certainly, the insurer and its agents are charged with knowledge of the instrument the insurance company drafts and the effect of its terms; Nationwide should know the legal consequences of its acts. Accordingly, the court holds that the insurance company did not mistakenly pay Borg-Warner.

In its earlier bench opinion, the court was persuaded by some dicta from a case arising out of the Seventh Circuit Court of Appeals that holds the defense of arson is not impliedly waived. *Lawndale Nat'l. Bank* v. *American Casualty Co.*, 489 F.2d 1384, 1388 (7th Cir. 1973). Upon further research and

consideration, the court concludes its previous decision was incorrect. In this diversity case a bank sued the insurance company to recover for fire losses to an apartment complex that the bank held in trust. The insurer raised the defenses of false statements and arson, and the trial court instructed the jury on both defenses. Since the court incorrectly instructed the jurors on the misrepresentation defense and the panel returned a general verdict for the defendant, the Seventh Circuit reversed the judgment and remanded the case for a new trial. *Id.* at 1389. The appellate court stated, in dicta:

> It is true that certain insurance defenses may be waived by an insurer *if not timely raised*, but not true of the defense of arson. Public justice, in our opinion, overcomes Lawndale's technical argument in this case. Arson is pregnant with danger to persons not privy to the insurance contract, a criminal act which in Illinois is classified as a "forcible felony." Arson is an act which transcends the insurance policy and has the potential of harm to innocent persons.

Id. at 1388 (emphasis added). The plainiff contends that *Hartford Fire Ins. Co.* v. *Mutual Savings & Loan Co.* is instructive on this issue. In the case discussed above, the insureds filed a proof of loss stating that they were the sole owners of the car and that there were no liens against the vehicles. In reliance upon this false statement the insurance company paid them. 193 Va. at 271, 68 S.E.2d at 542-43. As the plaintiff argues, this act constitutes the crime of obtaining money under false pretenses in Virginia and is punishable by imprisonment for one (1) to twenty (20) years or fine of not more than $1,000 or jailed for no more than twelve (12) months. Va. Code § 18.2-178 (Repl. Vol. 1982). Even though the Virginia Supreme Court has not addressed the issue at bar, the state court has held implicitly that a criminal defense may be waived by paying a loss payee under the policy.

Following this concrete Virginia case law, this court concludes that Nationwide clearly waived its defense of misrepresentation of material facts when it paid Borg-Warner

Acceptance Corporation. Moreover, the insurance company waived the defense of arson. The precedent is clear that if an insured pays a loss under the policy, it has waived a right of forfeiture about which it had knowledge. Arson is no exception. The Seventh Circuit case is based upon the law of Illinois and is not persuasive upon a court which must follow the precedent of the Virginia Supreme Court. The court is of the opinion that the state court would hold that both defenses were waived upon payment of Borg-Warner. Accordingly, the previous Order dated May 8, 1984, is vacated in part and the plaintiff's motion for partial summary judgment is granted.

The defendant has filed a motion to alter or amend this judgment pursuant to Rule 59(e) of the Federal Rules of Civil Procedure accompanied with an affidavit of Howard C. McElroy and a certificate of insurance. This certificate states, in part, that "[t]his insurance only as to the interest therein of B[org]-W[arner] A[cceptance] C[orporation] or its assignees, shall not be impaired or invalidated by any act or neglect of the insured, ..." Thus, the defendant argues that it paid Borg-Warner based upon its liability under this policy, not out of a mistake as to the legal significance. This action strengthens the court's factual findings that the insurer intentionally paid the co-loss payee and does not change the resulting forfeiture of the defenses against A & E. Accordingly, the defendant's motion to alter or amend is denied.

A & E SUPPLY COMPANY, INC.,
Plaintiff,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,
Defendant.

Civ. A. No. 81-0140-B.

United States District Court,
W.D. Virginia,
Big Stone Gap Division.

June 21, 1985.

MEMORANDUM OPINION

GLEN M. WILLIAMS, District Judge.

This is a suit to recover damages for fire loss from the insurer. The plaintiff, A & E Supply Company, Incorporated (A & E), seeks both compensatory and punitive damages. Originally instituted in Buchanan County, Virginia, this diversity action was removed before the Virginia Supreme Court announced its decision in *Kamlar Corp.* v. *Haley*, 224 Va. 699, 299 S.E.2d 514 (1983). Prior to trial, A & E moved this court for leave to amend its complaint to comply with *Kamlar*. *Kamlar* allows a plaintiff to set forth, in separate counts, allegations of independent, willful torts in order to support an award of punitive damages. *Id.* The court initially denied the motion to avoid further delay in bringing the case to trial. However, when the trial was continued by agreement of the parties, A & E was permitted to amend to allege independent, willful torts if said torts were supported by the facts alleged in the original complaint.[1]

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[1] Among the separate independent, willful torts pled by A & E in the amended complaint was the tort of slander. The court denied the motion to allow the allegation of slander because it was not mentioned in the original suit. Slander was proven by strong evidence and the court is now of the opinion that error was committed by not permit-

Partial summary judgment was granted to A & E prior to trial because Nationwide had already paid the claim of Borg-Warner Acceptance Corporation, a co-loss payee named in the insurance contract. The court held that payment to a co-loss payee waived the defenses of arson and misrepresentation. *A & E Supply Company* v. *Nationwide*, 589 F.Supp. 428 (W.D.Va. 1984). The total coverage of fire insurance on the building was $150,000. Nationwide paid the mortgagee named in the policy the sum of $117,930.21, leaving a balance of $32,069.79 as the maximum amount A & E could recover in actual damages for its loss. The total fire loss coverage on the contents of the building was $250,000. Of this amount, Nationwide paid Borg-Warner the sum of $61,033.91, leaving a balance of $188,966.09 as the maximum that A & E could recover for the loss of the contents. The jury was instructed that the most A & E could recover as compensatory damages was $32,069.79 for damage to the building and $188,966.09 for damage to its contents, a total of $221,035.88. The jury awarded the full amount of compensatory damages and also awarded the entire amount sought for punitive damages, $500,000.

Nationwide admitted at trial that the lost value of the building exceeded the amount of coverage. Therefore, there was no question that the sum of $32,069.79 was justified as an award for the balance of the loss of the building. The value of the building's contents was disputed. This dispute raised the question of whether goods and contents alleged to have been in the building at the time of the fire were actually there. Evidence of an overvalued inventory was used to support Nationwide's

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ting A & E to amend its complaint in view of the change made by the *Kamlar* decision. There was undisputed evidence that the defendant, Nationwide Mutual Fire Insurance Company, told creditors that A & E had deliberately burned its building to collect on the insurance policy. It was further shown that this slander was damaging to A & E, preventing the commencement of any new business and severely limiting its ability to obtain credit.

theory that the crime of arson had been committed by the owners. The issue of arson was thus placed directly before the jury. The verdict was based on certain interrogatories submitted by the court. The jury was required to find the amount of the actual loss of the building and the actual loss of its contents to arrive at the total for which compensatory damages were awarded. The court also asked the jury to decide whether the defendant had committed the torts of conversion, fraud or bad faith and whether the defendant had committed specific practices prohibited by the Unfair Trade Practices Act of Virginia.

This case is now before the court on Nationwide's motion for judgment notwithstanding the verdict or for a new trial. The motion is based on the following arguments: (1) that there was no finding, and indeed no proof, of compensatory damages for the separate independent torts and that punitive damages could not be awarded absent a finding of compensatory damages for the torts, (2) that A & E failed to prove the specific torts, (3) that the tort of bad faith is not legally cognizable in Virginia, (4) that, under Virginia Law, there is no implied private right of action for a violation of the Unfair Trade Practices Act, (5) that there was insufficient evidence to award punitive damages for lack of evidence showing actual malice or willful or wanton disregard by Nationwide of A & E's rights, (6) that there was no proof that Nationwide authorized or ratified the acts upon which A & E based its claims for the various torts, (7) that the punitive damages award was excessive and (8) that the evidence did not justify a finding of compensatory damages.

STATEMENT OF FACTS

In the late evening of Sunday, October 27 and continuing into the early hours of Monday, October 28, 1980, a fire completely destroyed the building and the contents of A & E Supply Company (A & E), a Virginia corporation, located in Buchanan County, Virginia. A & E was owned and operated by two brothers, Terry Lee Fletcher and Larry Fletcher. A & E was organized and incorporated in January, 1979 and operated as a

mine supply business. During its operation, A & E grew from monthly sales of $50,000 in January, 1979 to monthly sales of $275,000 for September, 1980. In the interim, during peak months sales had run as high as $334,000 per month. A & E's corporate fiscal year ended in November. At the direction of A & E's certified public accountant, an end of year inventory, which was almost 95% complete, was being conducted at the time of the fire. This inventory was introduced into evidence as Plaintiff's Exhibit Number 2; it recorded the amount that had been physically counted and projected the items which had not been counted. The total value of the recorded and projected inventory was $365,000, whereas the amount of insurance on the inventory was only $250,000.

Among the items shown on the inventory sheet were many highly inflammable items which would normally be totally destroyed in a fire. These included rubber tires, rubber rainsuits, plastic pipe, rubber splicing kits, rosin glue, rags, vinyl electric tape, rubber tape, paint, oil and grease, transmission fluid, rubber knee pads, compressed oxygen, rubber mine hose, etc. In addition to the inflammable items were items which would melt, such as bags of calcium chloride. There were, of course, numerous items which would not be consumed by fire, including copper wire, cables, metal buckets and items of that kind.

A & E's building was of double masonry wall throughout, consisting either of double brick or single brick and cinder block. The roof of the building was supported partly by metal I-beams and partly by wood rafters. Part of the roof was tin and part was tarpaper. During the course of the fire, the roof collapsed. Witnesses testified that a large area collapsed all at one time. This area was "almost the entire width of the structure and probably over half of its length." (Transcript I at 50). The portion that first collapsed was over the back of the building and later another part of the roof over the front of the building collapsed. In the areas where the roof collapsed, it covered the floor until the time this case was being tried and

made any effort to take an inventory most difficult, if not impossible. It was, of course, impossible to count any items which melted or which were inflammable and burned completely. Therefore, it was impossible to take an accurate inventory after the fire.

Many of the business records of A & E were destroyed by the fire. A & E later received certain cancelled checks and turned those over to Nationwide. They partially reconstructed the accounts receivable and accounts payable. Nationwide was provided an "aging sheet" which was current through September 30 but did not record the sales during the month of October. The accounts receivable at the end of September, according to the aging sheet, were $342,708. A & E was able to reconstruct $161,000 of invoices which had been given to customers and turned that information over to Nationwide. A & E contacted their suppliers after the fire, arranged to obtain records of what was owed to the suppliers and turned those records over to Nationwide. Individual tax returns of A & E's owners werer furnished to Nationwide. The insurance company refused to return the records to A & E even though they were requested many times. Nationwide advised A & E that it would be detrimental to its case to return any of the material requested. A & E was unable to complete its tax returns and got records from Nationwide only a few weeks prior to trial pursuant to a court order. The evidence is undisputed that A & E had made a written demand upon Nationwide which was specifically denied by a letter from District Claims Manager Robert Allen, who advised that the records would not be returned because it would be contrary to the best interests of Nationwide.

The only evidence placing any employee or either owner of A & E near the building for at least 48 hours before the fire showed that one employee entered the store on Saturday morning to make a delivery. The business was closed on Friday afternoon and the fire occurred on Sunday night. Nationwide produced no evidence, either by eyewitness testimony or cir-

cumstantial evidence, to show any opportunity of A & E's principals or agents to set the fire. Indeed, Nationwide made no attempt to confirm or refute the testimony of A & E's officers and agents about where they were before the fire.

After the fire, A & E forwarded its largely completed year-end inventory to Borg-Warner Acceptance Corporation. Borg-Warner furnished a copy to Nationwide and, in reliance thereon, some seven months after the fire Nationwide paid Borg-Warner as a loss-payee. Nationwide, however, refused to accept the inventory when considering payment of A & E's claim. Instead, they relied upon a physical count inventory taken at the scene of the fire despite the facts that the roof had fallen, making it impossible to inventory the items which were in areas where the roof had collapsed, and that a physical count was impossible because items were completely consumed by the fire.

Nationwide immediately employed Double K Investigative Services to determine the cause and origin of the fire. Kenneth Collins and Kenneth Riddleburger conducted the investigation. They determined that the fire originated in the left rear corner of the building and was caused by accelerants being poured on a concrete floor and ignited. There were numerous eyewitnesses present at the scene immediately after the fire was discovered who unanimously testified that the first visible fire was in the front of the building near some electrial switch boxes. An outside clock had stopped at 9:15. The clock was wired to a switch box in the area where fire was initially disocvered by the first people who arrived at the scene. None of the witnesses who observed the fire closely saw any fire where Nationwide's investigators placed the origin. Only one witness supported Nationwide's claimed point of origin; that was a woman who lived across the street. She was observing the fire from that vantage point when it first broke through the roof. The investigators for Nationwide immediately decided that arson had been committed. However, neither Nationwide nor its agents reported arson or the suspicion of arson to the proper

law enforcement agencies as required by the Arson Immunity Reporting Act. Instead, Nationwide concealed what it contended was a crime and thereby prevented competent arson investigators, fire marshals and other law enforcement officials from making a full investigation. While Nationwide had already decided to contend that arson had been committed, they represented that a settlement would be forthcoming if A & E would forward its financial records. Despite the fact that Nationwide from the beginning had no intention of paying the claim, they did not notify A & E until well into November that they suspected arson.

Although A & E had been having a cash flow problem and at times lacked sufficient funds to pay all its debts, it had an understanding with the bank that checks would be held until deposits were made to cover payment. After the fire, Nationwide submitted letters to the bank, Borg-Warner and various suppliers accusing A & E of committing arson. That put A & E in a position of being unable to get credit. The effect of these letters was to create a powerful incentive to force A & E to settle for a sum substantially less than the policy limits in order to avoid the cost of litigation. By the same token, Nationwide delayed payment to Borg-Warner for a period of seven months and delayed paying Cumberland Bank and Trust Company which had a mortgage on the realty. Nationwide also cancelled A & E's policy, making it difficult for them to obtain insurance elsewhere.

At trial, Nationwide, through its own accountant and other witnesses, admitted that its physical count inventory, the basis for all the accounting data which it had assembled, was inaccurate. In addition, Nationwide waited until the time of trial to stipulate that the damage to the structure exceeded the policy limits, notwithstanding its own real estate appraiser's opinion to that effect, which Nationwide had received well in advance. Not only did all eyewitnesses who were close to the fire dispute the point of origin determined by Nationwide's experts, but the plaintiff presented overwhelming evidence that the fire began

in the front of the building as the result of short circuits in the electrical wiring.

In May, 1981, Nationwide offered to pay A & E the sum of $232,000; A & E refused that offer. Shortly after A & E refused the offer to settle, a letter was issued by Nationwide denying the claim. The May, 1981 offer was the first and only offer made by Nationwide to A & E.

WHERE COMPENSATORY DAMAGES ARE SOUGHT AND OBTAINED FOR BREACH OF CONTRACT, IS IT ALSO NECESSARY FOR COMPENSATORY DAMAGES TO BE AWARDED FOR THE SEPARATE AND INDEPENDENT TORTS WHICH ARE ALLEGED IN CONNECTION WITH THE BREACH OF CONTRACT IN ORDER TO RECOVER PUNITIVE DAMAGES?

As previously noted, A & E recovery was $32,069.79 for the building and $188,966.09 for damage to contents. These amounts represent the difference between what was paid to the mortgagee and loss-payee, respectively, and the total amount of insurance. No compensatory damages were sought in the amended complaint for any injury due to tort. Separate and independent torts were alleged in order to support a claim for punitive damages, as required by *Kamlar*, 224 Va. at 699, 299 S.E.2d 514. There is no question that Virginia Law requires that compensatory damages be awarded before there can be an award of punitive damages for the torts. *Zedd* v. *Jenkins*, 194 Va. 704, 74 S.E.2d 791 (1953). Defendant contends that when a suit is brought for breach of contract and separate counts allege willful independent torts, there must be additional injury, separate and apart from damages caused by the breach, resulting from the independent torts before punitive damages can be awarded in the breach of contract action. *See Moffet* v. *Kansas City Fire Marine Insurance Co.*, 173 Kan. 52, 244 P.2d 228 (1952). Thus, the defendant argues that even if independent torts were alleged and proven, no injury or damages were proven to have resulted from the

separate independent torts so punitive damages cannot be awarded.

The answer to this question lies in the interpretation of *Kamlar Corp.* v. *Haley*, 224 Va. at 699, 299 S.E.2d 514. Prior to *Kamlar*, the United States Court of Appeals for the Fourth Circuit had interpreted Virginia Law to be that punitive damages would be available for breach of contract where the breach amounted to an independent willful tort due to malicious, wanton or oppressive behavior by the breaching party. *See Matney* v. *First Protection Life Insurance Co.*, 73 F.R.D. 696 (W.D.Va. 1977); *National Homes Corp.* v. *Lester Industries, Inc.*, 336 F.Supp. 644 (W.D.Va. 1972). In a contract action by the United States against a former C.I.A. agent for breach of a secrecy agreement, the Court of Appeals stated that punitive damages could be recovered "where the acts constituting the breach also constitute the commission of a tort or are closely analogous thereto." *United States* v. *Snepp*, 595 F.2d 926, 936 (4th Cir. 1979) *aff'd in part, reversed in part on other grounds*, 444 U.S. 507, 100 S.Ct. 763, 62 L.E.2d 704 (1980). The cases cited adhere to the rule of *Wright* v. *Everett*, 197 Va. 608, 90 S.E.2d 855 (1956).

It is obvious that the law as expressed in *Kamlar* by the Supreme Court of Virginia was not the law prior to the October 1, 1977 change in the Code of Virginia expressly permitting the joinder of tort with contract in a single pleading. Va.Code § 8.01-272 (1984 Repl.Vol.). *Kamlar*, therefore, marked a significant change in Virginia Law. *Kamlar* specifically recognized that since the law no longer required an election between tort and contract, a plaintiff seeking punitive damages in a breach of contract action could support the punitive damages claim by alleging a "wilful, independent tort." The court said.:

> [A] Plaintiff seeking punitive damages should allege a wilful, independent tort in a count separate from that which alleges a breach of contract. This serves to notify the defendant of the precise allegations he must meet at trial to resist that part of the claim which supports punitive damages. It also permits that aspect of the case to

> be tested separately from the rest, upon demurrer as to the sufficiency of the pleadings and upon a motion to strike as to the sufficiency of the proof.

224 Va. at 707, 299 S.E.2d at 518.

It is important to note what the court did not say; it did not require proof of damages from the separate independent tort nor did it require a plaintiff to seek compensatory damages for the separate independent tort. *Kamlar* holds that, in order to obtain punitive damages, one must allege and prove a separate independent tort. The dissenting opinion clarifies the holding of the majority. It is the court's understanding, based upon the majority opinion as modified by the dissent, that Nationwide's reliance on *Kamlar* is misplaced. The dissenting opinion states as follows:

> [T]he majority now says that the rule of [*Wright* v. *Everett*] 'require[s] proof of an independent, wilful tort, beyond the mere breach of a duty imposed by contract, as a predicate for an award of punitive damages, regardless of the motive underlying the breach.' As I understand that holding, proof of conduct which merely 'amounts to' a wilful tort without actually supporting an independent cause of action in tort will no longer suffice for recovery of punitive damages in a suit for breach of contract.

224 Va. at 711, 299 S.E.2d at 520 (Compton, J., dissenting).

The dissenting opinion then goes on to state:

> We are even advised by the majority that henceforth such a claim in tort should be pled in a count separate from that which alleges a breach of contract. This is a further indication, I submit, that no longer in Virginia will punitive damages be allowed in a pure contract action in which the proof shows conduct that evinces malice, wantonness or oppression.

Id.

Therefore, the court holds that it is proper to award punitive damages where there is an award of compensatory damages for breach of contract accompanied by proof of an independent,

willful tort beyond the mere breach of a duty imposed by the contract. However, there is a standard of proof that must be met before punitive damages can be awarded in any case. The jury was instructed that, if it found a tort or torts, punitive damages could be awarded only if the Virginia standard for punitive damages had been met by the evidence.

Defendant relies upon language in the recent case of *Gasque* v. *Mooers Motor Car Co.*, 227 Va. 154, 313 S.E.2d 384 (1984). *Gasque* cites *Kamlar* as holding that "[p]unitive damages are unavailable in suits purely *Ex Contractu*, and can be awarded only where an independent, wilful tort is alleged and proved." *Gasque*, 227 Va. at 159, 313 S.E.2d at 388. That is a correct statement of *Kamlar* which is in accordance with the ruling of this court. However, defendant relies upon the following language to assert that compensatory damages must be awarded for the tort before there can be an award of punitive damages:

> Even if the buyers' bill alleged a tort, which it fails to do, an award of compensatory damages, which are not claimed here, is an indispensible predicate for an award of punitive damages, except in actions for libel and slander.

Gasque, 227 Va. at 159, 313 S.E.2d at 388, *citing Newspaper Publishing Corp.* v. *Burke*, 216 Va. 800, 805, 224 S.E.2d 132, 136 (1976).

In *Gasque*, suit was brought for rescission of a contract. The prayer was for restoration of the parties to the *status quo ante*, including incidental damages. There was also a prayer for punitive damages, but the suit did not seek compensatory damages. The plaintiff, as the court pointed out, could have sought rescission of the contract and damages for the breach since the U.C.C. no longer requires an election of remedies between rescission and damages. The point, however, is that the plaintiff did not seek compensatory damages for breach of contract. The court simply said that compensatory damages must be awarded before punitive damages can be awarded. It did not say that the compensatory damages had to be for tort rather than for breach of contract. The defendant here is

clearly attempting to read into *Kamlar* something which the majority did not say and which the minority did not interpret it to say.

TORT OF CONVERSION

In *Buckeye National Bank* v. *Huff and Cook*, 114 Va. 1, 11, 75 S.E. 769, 772 (1912), the Virginia Supreme Court, quoting other authority with approval, defined conversion as "any wrongful exercise or assumption of authority, personally or by procurement, over another's goods, depriving him of their possession." Also, in *Universal C.I.T. Credit Corp.* v. *Kaplan*, 198 Va. 67, 76, 92 S.E.2d 359, 365 (1956), *citing* 19 *Michie's Jurisprudence*, Trover and Conversion, § 4 at 27, the Virginia Supreme Court stated:

> Any distinct act of dominion wrongfully exerted over the property of another, and in denial of his rights, or inconsistent therewith, may be treated as a conversion and it is not necessary that the wrongdoer apply the property to his own use. And when such conversion is proved, the plaintiff is entitled to recover, irrespective of good or bad faith, care or negligence, knowledge or ignorance.

Nattionwide, in a written brief filed to support its motion for judgment n.o.v. or for a new trial, states that the only records of A & E which it obatined were certain original cancelled checks and bank statements for October and November, 1980. Nationwide contends that these were given to Mr. Willard, its independent contractor, and that no employee of Nationwide knew that he had these original records until May, 1984, after their return to A & E. Therefore, Nationwide argues that Mr. Willard, an accountant, had possession of the records and, accordingly, Nationwide could not be guilty of conversion.

This bald statement in Nationwide's brief simply is not correct. It is not in accord with the facts nor is it in accord with any interpretation of the facts. There is positive testimony that A & E turned over its cancelled checks to Nationwide after the fire. An aging sheet, by which representatives of A & E contacted customers to obtain invoices that had been mailed to the

customers for sales made prior to the fire, was given to Nationwide. The testimony was that "we (A & E) were able to reconstruct $161,000" from the invoices. In response to a question about whether they forwarded the information to Nationwide, the answer, "Yes, sir, we did," was given. There was also positive evidence that Larry Fletcher's income tax returns were furnished to Nationwide and were held after return was demanded. Regarding accounts payable, witnesses testified that A & E turned its records over to Nationwide. This testimony was that "when we received these accounts payable invoices or, in other words, bills that we owed, uh, we went ahead and provided them to the insurance company and, uh, we didn't have copies for ourselves."

Robert Lambert, A & E's bookkeeper, was called as a witness by Nationwide. Upon direct examination by Nationwide's counsel, Defendant's Exhibit 67 was introduced and Mr. Lambert was asked if he had submitted it to Mr. Willard. Mr. Lambert stated that he had. Exhibit 67 was identified by Mr. Lambert in the following manner: "This is the sales that we had left over from October. These were the invoices that customers brought in to us after the fire. It's not all. The rest of them that weren't priced were destroyed in the fire." Mr. Lambert was also asked to identify Exhibit 68 and he identified it as accounts receivable as of October 31, 1980. When asked whether he had provided it to Mr. Willard after the fire, his answer was, "Yes."

Terry Fletcher testified that Exhibit 2, the inventory taken prior to the fire, was turned over to Max Willard about twenty or thirty days after the fire. The evidence further discloses that after the records were forwarded to Willard a written demand was made to Nationwide by A & E to return the same. Correspondence was introduced from Nationwide's District Claims Manager, Robert Allen, advising A & E that "its records" would not be returned because to do so would be contrary to the best interests of Nationwide.

Conversion is the taking of personal property by one person and the repudiation by that person of the owner's rights, or the

exercise of dominion over the property by that person in such a way as to be inconsistent with the rights of the owner. In this case, there is evidence, almost undisputed, in which the jury could have found that Nationwide exercised dominion over and refused to recognize the right of A & E to A & E's own records until compelled to do so by court order.

There was additional testimony which characterized the conversion of A & E's records by Nationwide as reckless disregard for the rights of another. Had there been a finding of no other tort than conversion, the verdict should be sustained in this case. There was testimony from Nationwide's own witnesses that a meeting took place between Mr. Willard, the independent accountant employed by Nationwide to assemble the records and testify as an expert witness, Mr. Robert Allen, the District Claims Manager, and Nationwide's attorney. At that meeting, Mr. Willard recorded in his notes that the purpose of the meeting was to come up with records and a theory to show that A & E had a motive for committing arson.

At trial, Mr. Willard, appearing as Nationwide's expert accountant, did not testify from his own computations but from arbitrary figures provided by Nationwide's agent and counsel. The figures they provided had no factual basis. Willard presented the figures to the jury to attempt to show that A & E was in bad financial shape, that the inventory was far less than the insurance coverage and that, in order to recoup its huge debt, A & E had deliberately set the fire. The jury obviously did not believe this testimony but believed the overwhelming testimony that the value of the property in the building far exceeded the insurance coverage.

The court concludes that Nationwide kept A & E's records to be able to prove its own side of the case and to prevent A & E from proving its side. Since Nationwide had the records, A & E could not provide necessary materials to enable their own expert witness to disprove Nationwide's theories. This was not only bad motive on the part of Nationwide but also

willful and wnaton conduct which alone was sufficient to support an award of punitive damages.

FRAUD

In accordance with Virginia Law, the jury was charged that the burden of proof was on the plaintiff to prove fraud by clear and convincing evidence. *Mutual of Omaha Insurance Co.* v. *Dingus*, 219 Va. 706, 250 S.E.2d 352 (1979). The jury was further instructed that actual fraud is the intentional misrepresentation of a material fact with the intent to mislead another person and reliance by that person so that damage results. *Packard Norfolk, Inc.* v. *Miller*, 198 Va. 557, 95 S.E.2d 207 (1956). A misrepresentation was defined as an incorrect statement of an actual existing or past fact; a promise, an expectation or an opinion concerning the future is not a misrepresentation. The jury was instructed that a misrepresentation may result from silence or from suppression of facts. *Horner* v. *Ahern*, 207 Va. 860, 153 S.E.2d 216 (1967). The jury was further instructed that Nationwide had violated the Arson Reporting Immunity Act by failing to notify and authorized agency in writing of the material which suggested arson, developed in the course of Nationwide's investigation of the fire loss, and that if Nationwide, by suppression of facts, had made a material misrepresentation upon which A & E had relied to its detriment, then the jury could find Nationwide guilty of fraud. In a second interrogatory, the jury found that the defendant had committed fraud.

The court has carefully reviewed the evidence and finds that the plaintiff failed to prove fraud by clear and convincing evidence. The testimony of the two individuals who owned A & E Supply Company was particularly examined. Terry Fletcher testified that he was informed in the middle of November that the insurance company thought that the owners of the property had committed arson. (Tr. I at 97). He stated that, until then, there had been no indication of any problem about payment of the claim and that he would not have given the records to Nationwide if he had known Nationwide was contending that

he had committed arson. Fletcher stated that A & E had discharged no employees and had informed its creditors that they could expect to be paid. He further testified that Mr. Allen, a representative of Nationwide was there within a couple of days after the fire.

The testimony of Larry Fletcher was somewhat more detailed on this point than that of his brother. His testimony on direct examination is as follows:

> Q. Okay. What did the insurance company tell you the situation was going to be right after the fire?
>
> A. Uh, they were going to help us, and,
>
> Q. Who told you that?
>
> A. Mr. Robert Allen.
>
> Q. What did he tell you?
>
> A. Uh, I told him right after he came, just immediately after the fire, about the last day that he was there, I guess, that we needed some immediate financial assistance, 'cause we didn't have any income, and that my creditors were really getting uneasy. And, I asked him if there was anyway that they could go ahead and even give us partial coverage right now, give us partial money to help us to stay on a plea, and he said, 'I think we can help you.' And, I said, 'Well, within the next week, or two weeks, or when?' And, he said, 'Possibly.' And, I said, 'would it be okay if I go ahead and contact my creditors, that we would have some income coming in in the next couple of weeks?' And, he said, 'Yes.' And, I did, I stuck my neck out with my creditors and I told them that, and it didn't happen.
>
> Q. Well now, it was only the 27th that the fire occurred, and you said that on the 30th or thereabouts, you were already telling him that the creditors were uneasy. Were you having that much trouble with your creditors?
>
> A. No, sir.
>
> Q. Well, why three days after the fire were you already trying to get money to take care of your creditors?
>
> A. Well, naturally they knew that our business was totally destroyed, and they were wondering what my sit-

uation was, and I told them, you know, that I felt that we had, you know, the proper coverage, and we would be going again here, pretty soon. And, that we'd be back, you know, strong.

Q. Did you plan on going back in strong?

A. Oh, yes, sir.

Q. Did you fire any employees?

A. No, sir.

Q. Now, the insurance company didn't pay you anything. When did you find out, or what was the first indication you had, the insurance company wasn't going to help you continue?

A. Well, after I had contacted my creditors and told them, you know, that I felt like that we could have some money here within the next couple—I told them exactly what Mr. Allen said. And then I think it was into the second week after, I asked him in a week or two, I think I called Mr. Allen, I did call him, and asked him if, you know, if our claim, are we still going to be able to get some of the money. And, he said, 'No.'

Q. Did he explain to you, why?

A. No, sir. He just said, 'Things is under investigation.'

(Tr. I at 296-98).

The words of Mr. Allen were couched in the framework of "I think we can help you" or "possibly." Clearly, Mr. Allen stated no more than an expectation or opinion concerning payment in the future. His statement must be taken in context; if considered a promise, it was made during the first two weeks after the fire, while the fire was still under investigation. The insurance company could not have reasonably been expected to arrive at a final answer in that short period of time. Furthermore, A & E had a duty under its insurance contract to provide any records that it had following a fire loss. A & E therefore cannot claim that it submitted records in reliance upon some promise made by Nationwide.

This evidence of fraud is not solid evidence of the type required when the standard of proof is "clear and convincing." The court has reviewed the record and failed to find any evidence showing detrimental reliance by A & E upon Nationwide's failure to comply with the Arson Reporting Immunity Act. No such evidence has been indicated by A & E's counsel. While the violation of the Arson Reporting Immunity Act is evidence of the bad faith of Nationwide, it is insufficient to constitute fraud.

BAD FAITH

As recently as 1983, this court in an opinion by Judge Turk found no Virginia authority which either rejects or accepts a cause of action in tort for bad faith failure to pay insurance benefits. *Morgan* v. *American Family Life Assurance Co. of Columbus*, 559 F.Supp. 477, 482 (W.D.Va. 1983). Judge Turk concluded his study of the subject as follows:

> This court does not hold at this time that the Supreme Court of Virginia would recognize a cause of action in tort for bad faith failure to settle a first party insurance claim. Nevertheless, a court should be especially reluctant to dismiss a complaint that asserts a novel theory of liability.

Morgan, 559 F.Supp. at 483, *citing* 5 C. Wright and A. Miller, *Federal Practice and Procedure: Civil* § 1357 at 603 (1969).

Following the precedent of not dismissing a claim which alleges the tort of bad faith, particularly in view of the fact that Judge Turk wrote without benefit of the decision of the Supreme Court of Virginia in *Kalmar*, this court submitted to the jurt the issue of whether Nationwide had acted in bad faith by not settling A & E's claim. The jury found that Nationwide had acted in bad faith and allowed $500,000 in punitive damages. Accordingly, the court must now determine whether Virginia recognizes the tort of bad faith failure to settle an insurance claim.

An analysis of the *Morgan* opinion reveals that Judge Turk strongly states that the tort of bad faith failure to pay an

insured's claim exists in Virginia. He presents four reasons why the Virginia Supreme Court would recognize a cause of action in tort for bad faith failure to settle a first party insurance claim. The first is that many state courts throughout the country have held that the tort of bad faith arises from the implied duty of an insurer to deal fairly and to act in good faith in processing claims. Judge Turk cites case law from Indiana, Connecticut, South Carolina, Vermont, Oklahoma, Rhode Island and Wisconsin. *Morgan*, 559 F.Supp. at 482. This court finds it unnecessary to repeat the citations, except for those cases particularly analogous to the question presented here. In addition, the Alabama Supreme Court has recognized the tort of bad faith in first party actions where it can be proven that the insurer lacks a reasonable basis for denying the claim or intentionally fails to determine whether there is a lawful basis of denial. *Chavers* v. *National Security Fire and Casualty Co.*, 405 So.2d 1 (Ala. 1981).[2]

The second reason asserted by Judge Turk is his interpretation of *Aetna Casualty and Surety Co.* v. *Price*, 206 Va. 749, 146 S.E.2d 220 (1966). The specific factual issue presented to the Supreme Court of Virginia there involved the insured's bad

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[2] Other states which recognize the tort of bad faith failure to settle a first party insurance claim, arising from the implied duty of an insurer to deal fairly and act in good faith, include California, *Gruenberg* v. *Aetna Casualty and Surety Co.*, 9 Cal.3d 566, 108 Cal.Rptr. 480, 510 P.2d 1032 (1973), Florida, *Escambia Treating Co.* v. *Aetna Casualty & Surety Co.*, 421 F.Supp. 1367 (N.D.Fla. 1976), Illinois, *Roberts* v. *Western-Southern Life Insurance Co.*, 568 F.Supp. 536, 554-55 (N.D.Ill. 1983), Mississippi, *O'Malley* v. *United States Fidelity and Guaranty Co.*, 602 F.Supp. 56 (S.D.Miss. 1985) and Missouri, *Associated Photographers, Inc.* v. *Aetna Casualty & Surety Co.*, 677 F.2d 1251 (8th Cir. 1982).

Some states have codified the tort cause of action. These include Georgia at Georgia Code Annotated § 56-1206, Montana at Montana Code Annotated § 27-1-221 (1979) and Tennessee at Tennessee Code annotated § 56-1105a (1980 Repl.).

faith refusal to settle a third party claim against the insured for an amount within the insurance coverage. *Id.* The court stated that "A relationship of confidence and trust is created between the insurer and the insured which imposes upon the insurer the duty to deal fairly with the insured in the handling and disposition of any claim covered by the policy." 206 Va. 749 at 760-61, 46 S.E.2d 220 at 227-28 (citations omitted). Thus the Virginia Supreme Court has imposed a duty on a liability insurer to exercise good faith in the settlement of third party claims against its insured because of the special fiduciary relationship between the insured and the insurer. The same "rationale which imposses a duty on the insurance company to exercise good faith in the negotiation and settlement of third party claims is of equal but separate importance when an insured seeks payment of legitimate claims from his own insurance carrier." *Trimper* v. *Nationwide Insurance Co.*, 540 F.Supp. 1188, 1193 (D.S.C. 1982).

The third indication that the tort of bad faith exists is found in Restatement (Second) of Contracts § 205 (1981). The Restatement recognizes that every contract imposes a duty of good faith and fair dealing in its performance and enforcement, whether it is an insurance contract or any other type. *Morgan*, 559 F.Supp. at 483. The fourth reason that Virginia would recognize the special relationship between an insurance company and its insureds is the legislative enactment of a broad range of statutory controls over insurance companies. *See generally* Title 38.1, Code of Virginia. Virginia Code § 38.1-32.1 (1984 Supp.) provides that an insurer's bad faith denial of coverage entitles the insured to recover costs and attorney's fees arising from a civil case. In addition, the Code imposes the duty of good faith on insurers for prompt and equitable settlements of claims in which liability has become reasonably clear. Va.Code § 38.1-52.9(6) (1981 Repl.Vol.). The enactment in other states of laws such as Virginia has promulgated has influenced those courts to recognize first party actions for bad faith in handling insurance claims. *Christian* v. *American Home Assurance Co.*, 577 P.2d 899 (Okla. 1978); *Phillips* v.

Aetna Life Insurance Co., 473 F.Supp. 984 (D.Vt. 1979); *Trimper* v. *Nationwide*, 540 F.Supp. 1188 (D.S.C. 1982).

The Virginia General Assembly has enacted a statute which provides that the tort of bad faith faulure to pay a motor vehicle insurance claim of less than $500.00 justifies an award of double damages. Va.Code § 8.01-66.1 (1984 Repl.Vol.) In such cases, the judge decides whether to award double damages because cases involving less than $500.00 are usually brought in general district court and are not tried by a jury. The prohibition against acts of bad faith applies to claims between the insured and the insurer and to third party claims. *Id.* The double recovery is available upon a finding of bad faith. It is awarded as compensatory damages, not as punitive damages. In order to recover punitive damages, there must also be a finding of willful and wanton misconduct by the insurer. The important question here is whether Virginia recognizes the tort of bad faith failure to settle and insurance claim. The tort is implicit in the statutory scheme as well as having been recognized in the case law.

Some courts have interpreted statutes which impose penalties and attorney's fees on the insurance companies to show legislative intent to exclude a common law remedy for bad faith conduct. *Morgan*, 559 F.Supp. at 483, *citing Spencer* v. *Aetna Life and Casualty Insurance Co.*, 227 Kan. 914, 611 P.2d 149 (1980) and *Farris* v. *United States Fidelity and Guaranty Co.*, 284 Ore. 453, 587 P.2d 1015 (1978). However, the overwhelming majority of courts in the United States which have considered statutory schemes penalizing bad faith and which recognize third party claims for bad faith refusal to settle below policy limits have recognized an implied duty of the insurer to deal fairly and act in good faith in processing claims.

A minority of the courts in the United States recognizes the duty to deal fairly with a third party claimant but holds that the relationship of confidence and trust which creates that duty does not exist between an insurer and its insured. *Id.* at 482. The Virginia Supreme Court, however, is clearly not a member

of that minority, having specifically stated that the duty to deal fairly exists in Virginia in "the handling and disposition of any claim." *Price*, 206 Va. at 761, 146 S.E.2d 220. The rule expressed in *Price* is in accord with Restatement (Second) of Contracts § 205 (1981) which requires good faith and fair dealing in every contractual situation. The Virginia Supreme Court recognizes a fiduciary relationship and requires good faith and fair dealing even in cases involving joint ventures, where there is no specific contractual relationship between the parties. *Witter* v. *Torbett*, 604 F.Supp. 298 (W.D.Va. 1984). Finally, Virginia's statutory scheme, which awards double damages plus attorney's fees in bad faith cases and double damages in other insurance cases supports recognition of the tort of bad faith more strongly than do the statutory schemes of most jurisdictions. For these reasons, Virginia would follow the majority rule and recognize the tort of bad faith failure to settle a claim in first party actions.

If there has ever been a case in which the facts justify a finding of bad faith by an insurance company adjusting a fire loss, this is the case. The evidence is almost undisputed that Nationwide acted in bad faith in handling A & E's claim. The following badges of bad faith are present in this case: (1) While Nationwide interviewed numerous witnesses including policemen, firemen and reputable citizens, it chose to completely ignore what those witnesses told its agents about the origin and location of the fire, relying instead upon one witness who viewed the fire from a very poor vantage point. (2) Undisputed evidence showed that the roof collapsed, covering most of the floor area over which the fire burned and that debris covered the floor in all the other areas. Yet Nationwide's investigators went to the scene, uncovered a small area of the floor and, due to some spaulding, designated the uncovered area as the point of origin. (3) Nationwide made no effort to determine whether a short circuit or other electrical problem caused the fire even though one piece of circumstantial evidence, a clock on the exterior wall, strongly suggested an electrical cause. The clock had stopped at fifteen minutes after nine P.M. The fire

was not discovered until about midnight, which might indicate that it had smoldered a long time, as opposed to Nationwide's theory of a sudden blaze which was deliberately set using gasoline. (4) Nationwide refused to accept the inventory which had been substantially completed for A & E's fiscal year ending November 1. Instead, Nationwide conducted its own inventory, counting those items which were visible and ignoring those which were covered or which had been completely destroyed. (5) Nationwide knew within days that its investigators would claim that arson was involved but never complied with Virginia Law which requires the reporting of suspected arson. Nationwide was attempting to construct a scenario in which they would have their evidence, but A & E would be unable to obtain any evidence of its own. The failure to report suspected arson prevented any government agency from making an investigation to determine whether arson had been committed. This violation of law was committed to gain an evidentiary advantage. That is the most plausible reason for having ignored the reporting statute, since Nationwide admitted that it was familiar with the law. (6) Shortly after the fire, Nationwide began to tell A & E's creditors that arson had been committed. This was done to destroy the credibility of A & E so that A & E could not go back into business. It was a tremendous act of bad faith intended to create a settlement advantage for Nationwide. The evidence of arson when Nationwide began to inform A & E's creditors was marginal at best. Even if the evidence had been substantial, Nationwide acted improperly in telling creditors who could have helped A & E get back into business that the fire was of suspicious origin. (7) The offer made by Nationwide five or six months after the fire was calculated to be the amount that A & E could hope to obtain if awarded a verdict for everything that they claimed. Undisputed testimony showed that the normal costs of a lawyer, excluding any costs for expert witnesses and investigation that would be involved, subtracted from the maximum amount recoverable under the policy, would be approximately the amount that Nationwide was willing to offer A & E to settle

the case. (8) Nationwide hired an accountant for the sole purpose of fabricating and substantiating at trial a theory to explain why A & E might burn its own building. In other words, Nationwide hired a supposedly independent accountant, furnished him with figures known to be inaccurate and required him to use those figures, which had no factual basis. At trial, the accountant admitted that the figures had been furnished by Nationwide and that he could not justify or swear to the accuracy of any of them. (9) Nationwide eventually paid Borg-Warner Acceptance Corporation based upon A & E's inventory, yet refused to use the same inventory to settle with A & E. (10) Nationwide's actions fell short of fraud. Nevertheless, Nationwide led A & E astray by words which could have been taken as encouragement, causing A & E to believe that a settlement would be forthcoming. Nationwide thus prevented A & E from adequately preparing for trial during the crucial time when an investigation could have been conducted more accurately and made it far more difficult for A & E to present its case. (11) While accusing the principal owners of arson, Nationwide made no effort to investigate their whereabouts at the time of the fire so as to either confirm or refute their statements. (12) By delaying payments to Borg-Warner Acceptance Corporation and Cumberland Bank and Trust Company for seven and nine months, respectively, and by delaying payment to A & E, Nationwide created an unfair incentive for A & E to settle for a sum significantly smaller than that due under the policy. (13) The fact that Nationwide waited until after the trial to admit that the building had greater fair market value than the amount of coverage was an extreme act of bad faith. (14) Nationwide cancelled A & E's policy after the fire. Cancellation was designed to position A & E so that it needed to settle in order to resolve the insurance problem. A & E was also placed in a difficult position to begin a new business. This placed A & E at a further disadvantage in settlement negotiations.

IS THERE AN IMPLIED PRIVATE RIGHT OF ACTION UNDER THE VIRGINIA UNFAIR TRADE PRACTICES ACT?

Virginia Code § 38.1-49 *et seq.* (1981 Repl. Vol.) prohibits numerous insurance practices. It is regulatory in nature and

empowers the State Corporation Commission to investigate and impose sanctions on persons who commit the prohibited practices. The sanctions include cease and desist orders, monetary penalties and revocation or suspension of licenses. The Virginia statute is based on a model act proposed by the National Association of Insurance Commissioners which has been adopted by at least 45 states. *Insurers and Third Party Claimants: The Limits of Duty*, 48 U.Chi.L.Rev. 125, 146 N. 75 (1981).

A & E's amended complaint alleges in Count VI that "[d]efendant was guilty of unfair trade practices and damaged plaintiff." Incorporated into Count VI are 26 previous paragraphs each alleging a factual basis for A & E's claim of unfair trade practices. This court held that a violation of the Unfair Trade Practices Act (Act) constituted a tort giving rise to a private cause of action. An interrogatory asked the jury to decide whether Nationwide had violated the Act, the answer was, "Yes." In instructing the jury, the court listed six practices prohibited by the Act and charged the jury that if any of those acts were committed by Nationwide with actual malice or with a willful and wanton disregard of plaintiff's rights then punitive damages could be awarded.[3]

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[3] You're further instructed that no person or corporation engaged in the business of insurance shall commit any of the following: (1) refusing arbitrarily and unreasonably to pay a claim; (2) not attempting in good faith to affectuate prompt, fair and equitable settlements of claims in which liability has become clear; (3) compelling the insureds to institute litigation to recover amounts due under an insurance policy by offering substantially less than the amount ultimately recovered in the action brought by such insured; (4) delaying the investigation or payment of claims by requiring an insured, claimant or the physician of either to submit a preliminary claim report and then requiring the subsequent submission of formal proof of loss forms both of which submissions contain substantially the same information; (5) failing to settle promptly claims where liability has become reasonably clear under one portion of the insurance policy coverage in order to influence settlement under other portions of the insurance policy coverage and (6) failing to provide promptly a

This court is bound by the precedent set in *Morgan* v. *American Family Life Assurance Co. of Columbus*, 559 F.Supp. 477 (W.D.Va. 1983), which stated, "Therefore, the court holds that the Supreme Court of Virginia would follow the reasoning in *Jenkins* and judicially imply a private cause of action in favor of insureds from the Virginia Unfair Trade Practices Act." *Id.* at 485.

This court believes that *Morgan* correctly applied the four-prong test for an implied private remedy set forth in *Cort* v. *Ash*, 422 U.S. 66, 78, 95 S.Ct. 2080, 2088, 45 L.Ed.2d 26 (1975). *Cort* v. *Ash* was subsequently strengthened by the language in *Cannon* v. *University of Chicago*, 441 U.S. 677, 99 S.Ct. 1946, 60 L.Ed.2d 560 (1978), when the Court stated that it "Has never withheld a private remedy where the statute explicitly confers a benefit on a class of persons and where it [the statute] does not assure those persons the ability to activate and participate in the administrative process contemplated by the statute." *Id.* at 707 n. 41, 99 S.Ct. at 1963 n. 41.

Morgan relies heavily on an interpretation of the West Virginia statute prohibiting unfair insurance practices, which is very similar to Virginia's Unfair Trade Practices Act. 559 F.Supp. at 484, *citing Jenkins* v. *J.C. Penney Casualty Insurance Co.*, 280 S.E.2d 252 (W.Va. 1981). For example, the West Virginia statute provides that administrative orders "shall [not] in any manner relieve or absolve any person affected by such order . . . from any other liability." W.Va.Code 33-11-6(c) (1982 Repl. Vol.). The Virginia statute states that "[n]o order of the Commission under this article shall in any way relieve or

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reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement. If you believe from the evidence that the defendant committed any of the foregoing acts and in doing so acted with actual malice toward the plaintiff or acted under circumstances amounting to a willful and wanton disregard of the plaintiff's rights, then you will award punitive damages in accordance with the other instructions of the Court.

absolve any person affected by such order from any liability under any laws of this Commonwealth." Va.Code § 38.1-57.1 (1981 Repl. Vol.).

While this court is bound and follows the *Morgan* holding, procedural problems remain. In *Jenkins*, the West Virginia court held that the underlying claim of the insured or third party against the insurer must be resolved before litigating the unfair practices claim. 280 S.E.2d at 259. The court stated that "[o]nce the underlying claim has been resolved, the issues of liability and damages have become settled and it is possible to view the statutory claim in light of the final result of the underlying action." *Id.* The California Supreme Court, for different reasons, mandates the same procedure. *Royal Globe Insurance Co.* v. *Superior Court*, 23 Cal.3d 880, 153 Cal.Rptr. 842, 592 P.2d 329 (1979). Virginia, however, allows contract and tort actions to be brought in one action. Va.Code § 8.01-272 (1984 Repl. Vol.). The manner of pleading is mandated by *Kamlar*, 224 Va. at 707, 299 S.E.2d at 518. The procedure used by A & E was proper. The Unfair Trade Practices Act implies a private right of action sounding in tort which can be tried along with the contract action for punitive damage purposes.

West Virginia also holds that more than a single violation must be proven in order to support any recovery. *Jenkins*, 280 S.E.2d at 259-60. The initial words of Section 33-11-4(9) provide that "no person shall commit or perform *with such frequency* as to indicate a general business practice any of the following. . . ." W.Va. Code § 33-11-4(9) (1982 Repl. Vol.) (emphasis added). For this reason, the West Virginia court concluded that multiple violations occurring in the same claim or proof of breaches in several other claims would support a private action. *Id.* at 260.

In Virginia, certain single acts may support a cause of action under the Unfair Trade Practices Act while other acts must occur frequently. Section 38.1-51 states that "[n]o person shall engage in this state in *any* trade practice which is defined in §§ 38.1-52.1 through 38.1-52.14 of the Code of Virginia as an

unfair method of competition or an unfair or deceptive act or practice in the business of insurance." Va. Code § 38.1-51 (1981 Repl. Vol.) (emphasis added). False, advertising, defamation, boycotts, intimidation, discrimination and rebates are examples of single act violations for which a person may be liable. However Section 38.1-52.9 contains the following language which is almost identical to the West Virginia statute: "No person shall commit or perform *with such frequency* as to indicate a general business practice any of the following. . . ." Va. Code § 38.1-52.9 (1981 Repl. Vol.) (emphasis added). In order to be consistent in following *Jenkins*, since the language used in the jury charge was taken from Va. Code § 38.1-52.9 (*see* Endnote 2), this court should have admitted evidence of frequency and instructed the jury accordingly. Nationwide objected when A & E offered evidence of other unfair practices of Nationwide; the objection was sustained. Nationwide also objected to the jury instruction given (*see* Endnote 3). While those objections were somewhat inconsistent, the court now believes that it erred in not permitting evidence of other unfair practices.

Having found, based upon the proof of Nationwide's conversioon and bad faith, that the jury award of compensatory and punitive damages was proper, the court considers the finding of violation of the Unfair Trade Practices Act to have been harmless error. Should a higher court find the other opinion in this case to be erroneous, this court would grant a new trial on the unfair trade practices claim.

SHOULD A & E RECOVER ITS COSTS AND REASONABLE FEES OF ITS ATTORNEYS BASED ON VIRGINIA CODE § 38.1-32.1?

On September 13, 1984, A & E petitioned the court to award its costs and attorney's fees. The ground proposed was Virginia Code § 38.1-32.1,[4] which grants a trial judge discretion to

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[4] § 38.1-32.2 Award of insured's attorney fees in certain cases.—

award costs and attorney's fees to an insured who proves at trial that his insurer "has not in good faith either denied coverage or failed or refused to make payment to the insured. . . ." Va. Code § 38.1-32.1 (Supp. 1984). Nationwide's answer included two broad arguments to support its position that the petition should be denied: (1) the statute is inapplicable to A & E and (2) the petition itself was not proper.

The court treats A & E's petition as a motion for relief from the final judgment and order entered on June 12, 1984. Fed. R.Civ.P. 60. Rule 60(b)(6) provides that on motion of a party and upon such terms as are just, a court may relieve a party "for any other reason justifying relief. . . ." *Id.* The rules provides that the motion must be made "within a reasonable time." *Id.* Because A & E's motion was timely filed the court will now consider its merits.

Nationwide proposes four arguments to show that Virginia Code § 38.1-32.1 is not applicable to A & E; only two are meritorious. The first is that A & E may not avail itself of the benefits of the statute because the statute, by its own terms, does not apply to corporations. Nationwide also contends that the statute does not apply retroactively.

The statute by its express terms applies to an "insured individual." Nationwide argues that a corporation is not within

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Notwithstanding any provision of law to the contrary, in any civil case in which an insured individual sues his insurer or his self-insurer to determine what coverage, if any, exists under his present policy or the extent to which his insurer is liable for compensating a covered loss, such individual insured shall be entitled to recover from the insurer costs and such reasonable attorney fees as the trial judge after verdict may award if it is determined by such trial judge in such case that the insurer has not in good faith either denied coverage or failed to refuse to make payment to the insured under such policy.

Nothing in this section shall be deemed to grant a right to bring an action against such insurance companies by an insured who would otherwise lack standing to bring action. (1982, c. 576.)

the definitional scope of an "insured individual." A & E urges that "individual" is interchangeable with "person." The correct definition of person, A & E contends, would include both natural and artificial persons and, therefore, corportions.

Title 38.1 of the Virginia Code contains all legislation concerning the insurance business in Virginia. Va.Code Title 38.1 (1950). Section 38.1-1 states definitions which are used throughout the title. No definition of "individual" appears. However, in the definitions given for "company" and "person", the words "individual: and "corporation" are included as part of the operative definitions. Va.Code §§ 38.1-1(4) and (11) (1981 Repl. Vol.). Nationwide cites *Jones* v. *Conwell*, 227 Va. 176, 314 S.E.2d 61 (1984) for the proposition that the words "individual" and "corporation" are both included because they have separate distinct meanings. The Virginia Supreme Court said in *Conwell:*

> The rules of statutory interpretation argue against reading any legislative enactment in a manner that will make a portion of it useless, repetitious or absurd. On the contrary, it is well established that every act of the legislature should be read so as to give reasonable effect to every word. . . .

Id. at 181, 314 S.E.2d at 64.

The court has examined other chapters within Title 38.1 and concludes that the legislature has intended the words "individual" and "corporation" to have separate distinct meanings. Section 38.1-52.14, which was repealed effective January 1, 1982, definied "[i]ndividual" as "any natural person who is a past, present or proposed named or principal insured. . . ." *Va.Code* § 38.1-52.14(3) (1981 Repl. Vol.). Section 38.1-57.5 defines terms used in Article 6.1, the Insurance Information and Privacy Protection Act. Va.Code § 38.1-57.5 (1981 Repl. Vol.). "Individual" is defined there as "any natural person. . . ." *Id.* The weight to be accorded these definitions is diminished because both are limited in application to their respective sections and because Section 38.1-52.14 has been

repealed. However, they serve as significant indicia of the legislature's intent to distinguish between individuals and corporations. In addition, a section within the same article as the cost and fees provision states, "No individual, partnership, corporation or association. . . ." *Va.Code* § 38.1-31.3 (1981 Repl. Vol.). That section clearly evidences an intent to encompass both individuals and corporations. Applying the *Conwell* reasoning, were individual and corporation read as synonymous, the legislature would necessarily have crafted a statute which is redundant. 227 Va. at 181, 314 S.E.2d at 64.

The legislature clearly intended to benefit natural persons when it used the language "insured individual." Va.Code § 38.1-32.1 (1981 Repl. Vol.). A & E argues that to limit the statute to natural persons is to discriminate unjustly and without reason against corporations. However, as Nationwide contends, it appears that the legislature enacted the statute as a form of consumer protection. Its purpose is to reimburse individual policy holders who, because of bad faith, are forced to sue their insurers to collect. Obviously, the legislature did not feel that corporations needed such protection.

The court finds that "individual" as used in Virginia Code § 38.1-32.1 includes only natural persons. *Id.* A & E, being a corporation, is therefore outside the coverage of the statute.

CONCLUSION

An Order will accordingly be entered denying defendant's motions for judgment n.o.v. and for new trial, entering final judgment on the verdict of the jury for the plaintiff, and denying plaintiff's petition for attorney's fees.

No. 86-1087

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

A & E SUPPLY COMPANY, INC.,
Petitioner,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY
Respondent.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

S. D. ROBERTS MOORE
W. CHARLES WADDELL, III
GUY M. HARBERT, III
GENTRY, LOCKE, RAKES & MOORE
P.O. Box 1018
Roanoke, VA 24005
Attorneys for Respondent

Of Counsel
HOWARD C. MCELROY
WHITE, ELLIOTT & BUNDY
P.O. Box 500
Abingdon, VA 24210

PRESS OF RAM PRINTING, HYATTSVILLE, MD 20781 (301) 864-6662

PARTIES BELOW

Respondent adopts the statement of the parties below contained in the Petition for Certiorari. However, in accordance with the Rules of the Supreme Court of the United States, respondent identifies the following as affiliated companies:

Nationwide Mutual Insurance Company
Nationwide Life Insurance Company
Nationwide General Insurance Company

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VIRGINIA STATUTES INVOLVED

Virginia Code Section 8.01-681 (Effective October 1, 1984) Decision of Appellate Court.—The appellate court shall affirm the judgment if there is no error therein, and reverse the same, in whole or in part, if erroneous, and enter such judgment as to the court shall seem right and proper and shall render final judgment upon the merits whenever, in the opinion of the court, the facts before it are such as to enable the court to attain the ends of justice. A civil case shall not be remanded for trial *de novo* except when the ends of justice require it, but the appellate court

shall, in the order remanding the case, if it be remanded, designate upon what questions or points a new trial is to be had. (Code 1950, Section 8-493; 1977, c. 617; 1984, c. 703.)

STATEMENT OF THE CASE

The petitioner, A&E Supply Company, Inc., instituted this action by the filing of a Motion for Judgment in the Circuit Court for Buchanan County, Virginia. Petitioner asserted causes of action based upon the breach of an insurance contract and the tort of "bad faith." Respondent, Nationwide Mutual Fire Insurance Company, then removed this case to the United States District Court for the Western District of Virginia.

Thereafter, petitioner moved to amend its Complaint and was permitted to add counts in which petitioner attempted to allege the torts of conversion, fraud, "obtaining property by false pretenses" and "unfair trade practices."[1] However, the District Court refused to permit the amendment to include the torts of trespass, intentional infliction of emotional distress and libel and slander inasmuch as facts underlying such causes of action were

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[1] This amendment was permitted in accordance with the decision of the Virginia Supreme Court in *Kamlar Corp.* v. *Haley*, 224 Va. 699, 299 S.E.2d 514 (1983). *A&E Supply Co. Inc.* v. *Nationwide*, 612 F.Supp. 760, 762 and n.1. (W.D.Va. 1985) (*See* Supp. App. p.9). Petitioner characterizes the holding of *Kamlar* as permitting recovery of punitive damages "for breach of contract where the breach amounts to an independent, willful tort." (Petition for Certiorari at 5, n.5). However, it is quite clear that the "independently willful tort" required by *Kamlar* must actually and independently constitute a separate cause of action. *Kamlar*, 224 Va. at 707, 299 S.E.2d at 517. Facts which merely "amount to," as opposed to actually constituting an independent cause of action in tort, are insufficient. *Id.*

not pled in the original Complaint. *A&E Supply Co., Inc.* v. *Nationwide*, 612 F.Supp. 760, 761-62 (W.D. Va. 1985) (*See* Supp. App. p. 9).

The case proceeded to trial upon the Amended Complaint and, after the District Court directed a verdict for the petitioner on the coverage issue, *A&E Supply* v. *Nationwide*, 612 F.Supp. at 762 (*See* Supp. App. p. 10); *A&E Supply Co., Inc.* v. *Nationwide*, 589 F.Supp. 428, 432 (W.D. Va. 1984) (*See* Supp. App. p. 8), the jury returned verdicts of $221,035.88 on the breach of contract claim and $500,000 for punitive damages only on the various tort claims. *A&E Supply*, 612 F.Supp. at 762 (*See* Supp. App. pp. 10, 11). Respondent moved for directed verdict, followed by motions for judgment notwithstanding the verdict or for a new trial on all counts. *Id.* at 762-63 (See Supp. App. p. 11). The District Court granted judgment notwithstanding the verdict on the fraud count. *Id.* at 770 (*See* Supp. App. p. 26). Respondent's remaining motions were denied. *See generally, A&E Supply*, 612 F.Supp. at 765-67, 770-73 (Supp. App. pp. 16-23, 26-32). Petitioner moved for attorney's fees pursuant to Va. Code Section 38.1-32.1, which motion was denied. *Id.* at 777 (*See* Supp. App. p. 39). Petitioner made no other post trial motions. However, the District Court conditionally ordered a new trial on the unfair trade practices issue. *Id.* at 775 (*See* Supp. App. p. 36).

Respondent appealed to the United States Court of Appeals for the Fourth Circuit only the judgment awarding punitive damages.[2] Petitioner cross-appealed only as

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[2] Respondent consciously chose not to challenge the decision of the District Court directing a verdict for the policy proceeds. Consequently, the judgment for $221,035.88 for the breach of contract was not appealed and the sum, plus interest and costs, has been paid.

to whether the District Court committed error in granting respondent judgment notwithstanding the verdict on the fraud count, in refusing to permit petitioner to amend its Complaint in order to increase its claim for punitive damages, in rulings relating to the unfair trade practices count, and in the denial of attorney's fees. Petitioner did not cross-appeal the District Court's dismissal of the torts of libel and slander, trespass and intentional infliction of emotional distress as improperly pled. The Court of Appeals reversed the punitive damages award and entered final judgment for the respondent on the tort counts. *A&E Supply Co., Inc.* v. *Nationwide*, 798 F.2d 669, 678 (4th Cir. 1986) (*See* App. p. 19a). The Court of Appeals affirmed the granting of judgment notwithstanding the verdict on the fraud count, *Id.* at 672 (*See* App. pp. 7a, 8a), and held that there was no private right of action under the Virginia Unfair Claims Practices Act.[3] *Id.* at 676 (*See* App. p. 14a). The court remanded the question of attorney's fees for further consideration by the District Court. *Id.* at 671, n.1 (*See* App. p. 3a, n.1).

Petitioner then petitioned the Court of Appeals for a rehearing and asserted for the first time that the absence of an award of compensatory damages on the tort counts entitled petitioner, under Virginia law, to a remand on that issue and that a new trial should be allowed so that petitioner could proceed on the defamation claim, inclusion of which by the way of amendment was denied by the District Court. *A&E Supply*, 612 F.Supp. at 762 (*See* App. p. 9a). The petition was considered by the Court of Appeals and was denied. Order filed September 26, 1986 (App. p. 20a). Petitioner now seeks a Writ of Certiorari from this Court upon these issues.

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[3] Va. Code Section 38.1-49 *et seq.*

SUMMARY OF THE ARGUMENT

The Court of Appeals did not misapply *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967) when it denied the Petition for Rehearing. When the Court of Appeals reversed the District Court's denial of judgment n.o.v. the new trial issues raised by the appellee, now petitioner, fell squarely within the discretion of the Court of Appeals. Based on the complete record before the Court of Appeals and its own experience with the case, it was in a position to dispose of the new trial ground on the slander claim without remand. Most importantly, under the circumstances, the fact that the slander claim was not litigated does not justify the award of a new trial. Since the slander claim was foreclosed by an adverse ruling by the District Court, the petitioner could not revive it when the Court of Appeals granted judgment n.o.v. to respondent without a cross-appeal. Petitioner cannot accomplish the revival of the slander claim by characterizing its motion as one for a new trial. The denial by the Court of Appeals of the Petition for Rehearing after granting judgment n.o.v. to respondent did not deny petitioner its Seventh Amendment right to trial by jury.

Furthermore, petitioner's argument that the Court of Appeals violated the holding of this Court in *Erie Railroad Co.* v. *Tompkins*, 304 U.S. 64 (1938) is clearly nothing more than an attempt to have this Court pass upon petitioner's novel interpretation of the Virginia law pertaining to punitive damages. Since there is nothing patently improper in the application of Virginia law by the Court of Appeals in this case, this issue does not rise to the level of importance so as warrant review by this Court.

ARGUMENT

I. THE COURT OF APPEALS IN DENYING THE PETITION FOR REHEARING AND DIRECTING THE DISTRICT COURT TO ENTER JUDGMENT FOR THE RESPONDENT WAS WELL WITHIN ITS JUDICIAL DISCRETION AND DID NOT MISAPPLY *NEELY* v. *MARTIN K. EBY CONSTRUCTION CO.* 386 U.S. 317 (1967).

Petitioner has failed to demonstrate any reason for this Court to exercise its discretion to review the denial by the Court of Appeals of petitioner's Petition for Rehearing and the request for new trial contained therein. Despite the suggestions by petitioner that this case presents an issue worthy of review, at the very best, the petition merely questions the exercise of discretion by the Court of Appeals in denying petitioner's request for a new trial on the separate slander claim. The Court of Appeals expressly stated in its Order that it considered the Petition for Rehearing and was of the opinion that it should be denied. *See* Order filed September 26, 1986, (App. pp. 20a, 21a). This petition does not involve a "misapplication" of *Neely* v. *Martin K. Eby Construction Co.*, 386 U.S. 317 (1967) or a departure from the accepted course of proceedings which demands the supervision of this Court.

The decision in *Neely* makes it clear that Rule 50(d), Fed. R. Civ. P., is permissive in nature in its direction to the Court of Appeals in handling new trial requests by an appellee after reversing a district court's denial of appellant's motion for judgment n.o.v. The appellee, petitioner in this case, may assert grounds, if any, for new trial to the Court of Appeals in its brief or by petition for rehearing. *Neely*, 386 U.S. at 329. Rule 50(d) provides adequate opportunity for an appellee to present its

grounds for new trial to the Court of Appeals in the event its verdict is set aside by the Court of Appeals. *Id.*

Neely further makes it clear that the consideration of the new trial question "in the first instance" is lodged with the Court of Appeals. There is nothing in Rule 50 which indicates that the Court of Appeals in its discretion may not deny the request for new trial and direct the entry of judgment n.o.v. in favor of the appellant. *Neely*, 386 U.S. at 324. "[T]he Court of Appeals may make final disposition of the issues presented, except those which in its informed discretion should be reserved for the trial court." *Id.* at 329.

In the instant case, petitioner filed an extensive petition for rehearing setting forth its arguments for a new trial on the issue of slander. Due to the nature of the respondent's appeal and the petitioner's cross-appeal, the entire trial transcript was before the Court of Appeals by joint appendix which included rather lengthy District Court opinions detailing the rulings of the Court and the factual basis for them. *A&E Supply* v. *Nationwide*, 589 F.Supp. 428 (W.D. Va. 1984) and *A&E Supply* v. *Nationwide*, 612 F.Supp. 760 (W.D. Va. 1985) (*See* Supp. App.) In accordance with *Neely*, the petitioner had a full and adequate opportunity to present its grounds for a new trial to the Court of Appeals for decision.

The Court of Appeals may make final disposition of issues presented for new trial except those which in "its informed discretion" should be reserved for the trial court. *Neely*, 386 U.S. at 329. Although the petitioner takes issue with the denial of its new trial ground by the Court of Appeals, it does not argue or suggest that the circumstances are such that the District Court was in a better position to decide whether a new trial was

approprite as opposed to the Court of Appeals. The Court of Appeals reversed the District Court and directed judgment n.o.v. in favor of the respondent on the basis of matters of law. The circumstances surrounding the slander claim were fully contained in the record. The decision by the Court of Appeals did not involve errors in the application of an evidentiary standard which might give rise to questions of sufficiency of the evidence had the proper standard been applied. *See Neely*, 386 U.S. at 327-29 (indicating that there may be circumstances justifying a remand). Based on the full record before the Court of Appeals and its own experience with the case, the Court of Appeals was in a position to consider the grounds asserted for a new trial and dispose of same without the necessity of remanding to the District Court.

In any event, contrary to petitioner's argument, the separate cause of action of slander did not provide petitioner with a valid ground for a new trial. It was not an alternative theory or contention of liability which had not been litigated under circumstances justifying the award of a new trial to petitioner. The separate cause of action of slander as well as separate causes of action of intentional infliction of emotional distress and trespass were claims which were dismissed by the District Court in advance of trial as improperly pled. *A&E Supply*, 798 F.2d at 671, (*See* App. p. 4a); *A&E Supply*, 589 F.Supp. at 429 (*See* Supp. App. p. 1); *A&E Supply*, 612 F.Supp. at 761-62 (*See* Supp. App. p. 9). Petitioner filed suit against respondent in April of 1981 and did not seek or file an amended complaint until May of 1984. *A&E Supply*, 589 F.Supp. at 429-30 (*See* Supp. App. pp. 1 and 2). The District Court dismissed the claims because those torts were not supported by the facts alleged in the original complaint. *A&E Supply*, 612 F.Supp. at 761-62 (*See* Supp. App. p. 9).

Under the circumstances presented, this was merely a situation where an appellee failed to raise an error by cross-appeal when an appellant pursued an appeal from the District Court's denial of its motion for judgment n.o.v. Had petitioner filed a cross-appeal on this point, the Court of Appeals would have reviewed the District Court's ruling on the slander claim.

Notwithstanding petitioner's attempt to create a *Neely* issue, respondent suggests that this situation represents nothing more than petitioner's choice to abandon the slander claim or failure to cross-appeal the adverse ruling by the District Court. The District Court seemed to invite the petitioner to file a cross-appeal when it questioned its pre-trial ruling. *See A&E Supply*, 612 F.Supp. at 762 n.1 (Supp. App. p.9, n.1). Petitioner declined, preferring to pitch its appeal on the claims tried before the jury and on the verdict obtained. The Court of Appeals specifically noted the fact that the petitioner did not cross-appeal on those claims. 798 F.2d at 671 (App. p. 4a). Further, petitioner argues as a reason for review that the circumstances unfairly deprived it of the opportunity to have either the trial court or jury pass on the merits of its slander claim. However, it is clear that any such deprivation is a direct result of petitioner's failure to properly plead the slander claim and/or subsequent failure to cross-appeal from the District Court's adverse ruling.[4]

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[4] The petitioner only argues for new trial on the basis of slander not having been litigated but the District Court's ruling also precluded the assertion of separate torts of intentional infliction of emotional distress and trespass. *A&E Supply*, 798 F.2d at 671 (App. p. 4a). Of further interest, petitioner did cross-appeal the District Court's adverse rulings relating to attorneys' fees, *A&E Supply*, 798 F.2d at 671, n.3, (App. 5a), fraud, *Id.* at 672, (App. p. 4a and Petition for Certiorari p. 6, n.6), and its request to amend in order to increase the amount of punitive damages sought. *Id.* at 671, n.2 (App. 4a, n.2).

Petitioner, apparently recognizing this problem, argues that it could not appeal or cross-appeal from a decision awarding everything sought in the District Court citing *New York Telephone* v. *Maltbie*, 291 U.S. 645 (1934). However, the principle has no applicability in circumstances such as the instant case where there is an obligation to cross-appeal when the appellant notes an appeal in the first instance. W. Moore, 9 *Moore's Federal Practice*, ¶204.11(3), pp. 4-43-4-53 and cases cited therein. If *Maltbie* applies, the judicial economy served by the requirement of cross-appeal would be virtually eliminated.

It is well recognized that appeal from a final judgment draws into question all rulings of the court which preceded that judgment. *See Roth* v. *Hyer*, 142 F.2d 227 (5th Cir. 1944), *cert. denied*, 323 U.S. 712 (1944); *Aaro, Inc.* v. *Daewoo International*, 755 F.2d 1398, 1400 (11th Cir. 1985); 2 Fed. Pro. Law. Ed. Section 3-445. Accordingly, when respondent, as appellant, noted its appeal in this matter, it was incumbent upon petitioner in order to be in a postion to revive its separate claim of slander dismissed by the District Court to cross-appeal. *Morley Construction* v. *Maryland Cas. Co.*, 300 U.S. 185, 191 (1936); *Swarb* v. *Lennox*, 405 U.S. 191, 201 (1972), *reh. denied*, 405 U.S. 1049; *United Optical Workers' Union* v. *Sterling Optical*, 500 F.2d 220, 224 (2nd Cir. 1974); *Stella* v. *DePaul Community Health Center Inc.*, 642 F.2d 258, 261 (8th Cir. 1981); *NLRB* v. *International Van Lines*, 409 U.S. 48 (1972).

Petitioner does not fall under the exception recognized in *Morley*, 300 U.S. at 191 and in subsequent cases, which allows an appellee, without filing a cross-appeal, *to support a judgment* awarded in the District Court with matters appearing in the record. Here, petitioner seeks *to*

attack the judgment of the District Court dismissing its separate claim of slander as improperly pled in order to enlarge its own rights. It has been recognized by this Court that an appellee, without filing a cross-appeal, may not defend the sum of a money judgment by asserting error in the District Court which, if corrected, might entitle it to a sum equal to or more than the amount of the judgment. If an appellee wishes to argue error of the District Court in denying a claim, it must file a cross-appeal. *Helvering* v. *Pfieffer*, 302 U.S. 247 (1937); *Alexander* v. *Cosden Pipeline Co.*, 290 U.S. 484 (1933); W. Moore, 9 *Moore's Federal Practice*, ¶204.11(3), pp. 4-46, 4-47, nn. 16 and 17.

Under these circumstances which were clearly presented to the Court of Appeals in the record, it could properly exercise its discretion in refusing to allow petitioner to re-open the matter pertaining to slander by cross-appeal or by seeking a new trial.[5] Petitioner failed to cross-appeal on the point. It could not seek the same relief by characterizing its motion as one for a new trial. Petitioner has received its proceeds under the policy as awarded by the jury. *A&E Supply*, 798 F.2d at 671 (*See* App. p. 5a). The Court of Appeals has rejected its attempts to recover punitive damages in this case. This disposition was within its discretion.

Finally, petitioner claims that the reversal of the District Court's denial of judgment n.o.v. and entry of judg-

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[5] In any event, it appears that the potential slander claim would have been barred by the applicable statute of limitations. *See Schoonfield* v. *Mayor and City Council of Baltimore*, 399 F.Supp. 1068, 1090 (D.Md. 1975), *aff'd.*, 544 F.2d 515 (4th Cir. 1976); *Also see Morrissey* v. *William Morrow & Co.*, 739 F.2d 962, 967 (4th Cir. 1984), *cert. denied*, 496 U.S. 1217 (1985) (recognizing Virginia's one year statute of limitation for defamation).

ment n.o.v. in favor of the respondent denied petitioner its Seventh Amendment right to trial by jury. (Petition for Certiorari at pp. 10-12). This contention is dismissed in *Neely*. 386 U.S. 317, 321-22. There is no constitutional bar to an appellate court directing the entry of judgment n.o.v. on appeal. *Id.*

II. THERE WAS NO VIOLATION OF THE *ERIE* DOCTRINE BY THE COURT OF APPEALS WHEN IT CHOSE NOT TO REMAND THIS CASE FOR A NEW TRIAL ON THE ISSUE OF CONVERSION.

A. The Court Of Appeals Correctly Concluded That Virginia Law Requires An Award Of Compensatory Damages As An Indispensible Prerequisite To An Award Of Punitive Damages.

Petitioner's conclusory statement that Virginia law does not require an award of compensatory damages before an award of punitive damages is permissible, and that the Court of Appeals violated the holding of this Court in *Erie Railroad Co.* v. *Tompkins*, 304 U.S. 64 (1938) when it imposed such a requirement, (Petition for Certiorari at 13), is simply without the support of the Virginia authorities. Indeed, the Virginia Supreme Court has passed upon the question on numerous occasions and has concluded that, as a general rule, "an *award* of compensatory damages . . . is an *indispensible predicate* for an award of punitive damages." *Gasque* v. *Mooer's Motor Car Co.*, 227 Va. 154, 159, 313 S.E.2d 384, 388 (1984) (emphasis added); *see also Valley Acceptance Corp.* v. *Glasby*, 230 Va. 422, 433, 337 S.E.2d 291, 297 (1985) (where "neither compensatory damages nor nominal damages were *awarded* . . . punitive damages could not be awarded") (emphasis added); *Fleming* v. *Moore*, 221 Va. 884, 893-94, 275 S.E.2d 632, 638 (1981) ("in conformity with the general rule in tort actions, no punitive

damages may be awarded for slander or libel *unless compensatory damages are awarded*") (emphasis added); *Newspaper Publishing Corp.* v. *Burke*, 216 Va. 800, 805, 224 S.E.2d 132, 136 (1976) ("the general rule in tort cases requires an *award of actual damages* as a prerequisite to an award of punitive damages") (emphasis added). The only instances under Virginia law where compensatory damages need not be awarded before punitive damages are recoverable are cases involving defamation *per se*. *Fleming* v. *Moore*, 221 Va. at 894, 275 S.E.2d at 638; *Burke*, 216 Va. at 805, 224 S.E.2d at 136. Since petitioner's argument that it is entitled to punitive damages is based upon the tort of conversion, the punitive damages award, unsupported by an award of compensatory damages, was fatally defective under Virginia law.

Petitioner relies upon *Zedd* v. *Jenkins*, 194 Va. 704, 74 S.E.2d 791 (1953) to support its argument on this issue. However, for two crucially important reasons, it is clear that this reliance is misplaced. First, petitioner argues that the language of *Zedd* permits a recovery of punitive damages to be based upon a "finding," as opposed to an "award," of compensatory damages. (Petition for Certiorari at 14). According to petitioner, this means that an actual monetary award of compensatory damages by the jury is not required. *Id.* However, this is contrary to the very language in that opinion. The Virginia Supreme Court specifically noted that the evidence in *Zedd* was "sufficient to sustain a verdict awarding plaintiff a reasonable sum for actual damages." *Id.* at 708, 74 S.E.2d at 793. Thus, under petitioner's interpretation there was a "finding" of entitlement to compensatory or actual damages. However, the court held that a plaintiff could not maintain an action for punitive damages only, *Id.* at 706, 74 S.E. 2d at 793, and that an award of punitive damages only, even

though accompanied by such evidence of actual damage, was illegal under Virginia law. *Id.* at 708, 74 S.E.2d at 793. Furthermore, the court instructed the jury that punitive damages were recoverable only if the jury first awarded compensatory damages. *Id.* at 707, 74 S.E.2d at 793, n.1. Since there was no actual monetary award of either compensatory or nominal damages, the court in *Zedd* held, in direct contrast to petitioner's argument, that there was no "finding" of compensatory or nominal damages and therefore the award of punitive damages could not stand. *Id.* at 708, 74 S.E.2d at 793. Ever since it was decided, *Zedd* has been interpreted as requiring the very opposite result from that which petitioner now urges. *See, e.g.*, *Durham* v. *New Amsterdam Casualty Co.*, 208 F.2d 342, 345 (4th Cir. 1953); *Valley Acceptance Corp.* v. *Glasby*, 230 Va. at 433, 337 S.E.2d at 297; *Newspaper Publishing Corp.* v. *Burke*, 216 Va. at 805, 224 S.E.2d at 136.

Second, Petitioner's attempt to analogize the present factual situation with the facts of *Zedd* fails. Petitioner argues that it presented at trial sufficient evidence to warrant a "finding" of entitlement to compensatory damages by the jury. (Petition for Certiorari at 13). However, it is quite clear from reading the opinion of the Court of Appeals that the court concluded that not only did petitioner fail to receive an actual award of compensatory damages, but also that plaintiff failed to prove that it was entitled to any such damages. The Court of Appeals specifically found, as a matter of law, that petitioner failed to present the necessary evidence that the dispossession in question "involved a palpable loss." *A&E Supply*, 798 F.2d at 673, (*See* App. p. 8a). The court further noted that the only damages which petitioner proved at the trial below were damages for breach of contract. *Id.* The court correctly concluded that such consequential damages for

breach of contract could not support an award of punitive damages for conversion. *A&E Supply*, 798 F.2d at 673, (*See* App. pp. 8a, 9a). Therefore, contrary to petitioner's arguments, not only did petitioner fail to receive an award of compensatory damages in order to support its award of punitive damages, it also failed to prove that it was entitled to any such award of compensatory damages in the first place. Even if petitioner's construction of the opinion of the Virginia Supreme Court in *Zedd* is somehow correct, petitioner is nevertheless still not entitled to punitive damages because it failed to prove that it suffered any loss as a proximate result of the tort.

Petitioner next relies upon the case of *Peacock Buick* v. *Durkin*, 221 Va. 1133, 277 S.E.2d 225 (1981) to support its position. (Petition for Certiorari at 13 and nn. 14 and 15). Petitioner argues that the Virginia Supreme Court in that case approved a jury instruction which permitted a verdict for punitive damages without an actual award of compensatory damages. *Id.* However, it is apparent that petitioner has examined only one small portion of just one of the jury instructions cited by the court and has assigned to it a significance which is completely unwarranted. When read as a whole the jury instructions at issue in the *Peacock Buick* case clearly informed the jury that punitive damages were something which it could award "in addition to compensatory damages." *Peacock Buick* v. *Durkin*, 221 Va. at 1137, 277 S.E.2d at 227, n.3. Furthermore, compensatory damages were actually awarded to the plaintiff in *Peacock Buick* and the Virignia Supreme Court never directly addressed the question of whether an award of compensatory damages was a necessary prerequisite to an award of punitive damages. However, in those cases where the court has directly addressed that question, it has, as pointed out above,

answered the question in the affirmative. Indeed, petitioner has not pointed to a single case in which only punitive damages were awarded for anything other than the tort of defamation *per se*.

The Court of Appeals, in concluding that an award of punitive damages only, without an underlying award of compensatory damages, was illegal under Virginia law, rendered a decision in accordance with and pursuant to Virginia law. Consequently, there was no violation of the *Erie* doctrine. Petitioner's argument to the contrary is nothing more than a thinly disguised attempt to bring a marginally debatable question of Virginia law within the purview of Rule 17 of Rules of the Supreme Court of the United States. Clearly, this attempt must fail.

B. The Decision Of The Court Of Appeals To Enter Final Judgment In Favor Of The Defendant Was Consistent With Virginia Law.

Petitioner argues, again based upon *Zedd* v. *Jenkins*, 194 Va. 704, 74 S.E.2d 791, that had the present case been tried in state court, petitioner would have been "entitled" to a remand on the issue of conversion in order to clarify the "ambiguity" created in the verdict by the jury's award of punitive damages only. (Petition for Certiorari at 14). However, it is clear that the decision not to remand is entirely consistent with Virginia law. If the Court of Appeals did not actually apply the Virginia law on this issue, it is quite clear that the court's application of federal law brought about a result so substantially similar to that which would have followed in state court that there was no violation of the *Erie* doctrine. *See Guaranty Trust Co.* v. *York*, 326 U.S. 99, 109 (1945).

The Virginia Supreme Court held in *Zedd* that remand in that case was proper pursuant to Va. Code Section

8-493 (1950). *Zedd* v. *Jenkins*, 194 Va. at 708, 74 S.E.2d at 793-94. That code provision, which exist today and existed at the time of this appeal to the Court of Appeals as Va. Code Section 8.01-681, provides that a remand is proper under Virginia law "when the ends of justice require it." Va. Code section 8.01-681. The court no doubt determined that "the ends of justice" required a remand in *Zedd*. However, that decision was made not only because the jury returned a verdict for punitive damages only, but also because the trial judge committed reversible error in instructing the jury foreman to delete the words "for punitive damages only" from the verdict. *Id.* at 707, 74 S.E.2d at 793. Such action by the trial judge created an ambiguity which made it impossible to determine whether a true verdict had been rendered. *Id.* In the present case, if an "ambiguity" indeed exists, it was brought about solely by the petitioner's failure to even ask for compensatory damages for the alleged conversion. Since the District Court committed no improper act which gave rise to an ambiguous verdict, *Zedd* does not require a remand in the present case.

Furthermore, had this case been litigated in state court and the Virginia Supreme Court had confronted the issue of remand, that issue would have been determined in accordance with the following statement of that court:

> The question of whether final judgment should be entered or the case remanded for trial *de novo*, or upon designated questions or points, lies largely in our discretion, and depends upon the facts and circumstances of the case. Before entering final judgment, it should be reasonably apparent that the case has been fully developed in the trial court, or at least, that the parties had a fair opportunity of so developing the case, and we must be of the opinion that, upon the facts before us, the parties have had a fair trial on

> the merits of the case, and that substantial justice has been reached.

Kearns v. *Hall*, 197 Va. 736, 744, 91 S.E.2d 648, 653-54 (1956). There is no doubt that the petitioner had a fair opportunity to try its case in the District Court. Again, the primary reason no compensatory damages were awarded is the fact that petitioner sustained no compensable loss and never asked the court or the jury for such relief. It certainly cannot be said that the Court of Appeals violated the above guidelines or abused its discretion when it chose to enter final judgment in favor of the respondent.

Finally, any doubt as to whether petitioner was guaranteed or entitled to a remand under Virginia law is erased by the decision of the Virginia Supreme Court in *Valley Acceptance Corp.* v. *Glasby*, 230 Va. 422, 337 S.E.2d 291 (1985), which was rendered during the pendency of the appeal of this case to the Court of Appeals. In *Valley Acceptance*, the court held that a punitive damages award was improper absent an award of compensatory or nominal damages and reversed the judgment in favor of the plaintiffs on the issue of punitive damages. Significantly, no remand was ordered. Indeed, no remand was ordered despite the court's observation that the evidence revealed "wrongdoing" on the part of the defendant, *Id.* at 433, 337 S.E.2d at 297, and that the plaintiffs had incurred some pecuniary loss as a result of this wrongdoing. *Id.* at 425-26, 337 S.E.2d at 293. Obviously, the Virginia Supreme Court in that case concluded that "the ends of justice" did not require a remand under those facts. There is no reason to believe that the same court would not have reached the same conclusion in this case.

C. The Court Of Appeals Correctly Concluded That Petitioner Failed To Present At Trial Evidence Sufficient To Support A Judgment For Punitive Damages Based Upon The Tort Of Conversion.

Finally, it is apparent that the petitioner has incorrectly assumed that the Court of Appeals determined that the evidence on the issue of conversion was sufficient to establish actual malice on the part of the respondent so as to otherwise entitle the petitioner to punitive damages. However, it is quite clear that the Court of Appeals determined that the award of punitive damages was improper not only because of the absence of an award of compensatory damages, *A&E Supply*, 798 F.2d at 673 (*See* App. p. 8a), but also because the evidence at trial was insufficient to establish liability for punitive damages. *Id.* at 673 (*See* App. p. 9a). Specifically, the Court of Appeals observed:

> Nationwide did not refuse to return the A&E records until April 29, 1981, more than six weeks after Nationwide had formally rejected the insurance claim. The wrongful retention of property was not factually bound to the breach [of contract] but to the efforts of Nationwide to prove its position in the ensuing litigation. A&E did not request the return of documents until it had initiated suit. It would undermine the rule of *Kamlar Corp.* v. *Haley* [224 Va. 699, 299 S.E.2d 514] if subsequent disputes over evidence were to translate into the tort of conversion *sufficient to support a punitive damages award* in an action for contractual breach.

A&E Supply, 798 F.2d at 673 (*See* App. pp. 8a, 9a) (Emphasis added).

Therefore, irrespective of whether the Court of Appeals applied the correct Virginia law on the issue of whether an award of compensatory damages must be

made in order to support an award of punitive damages, the court correctly concluded that punitive damages were not warranted by the facts of this case. Since punitive damages were not recoverable on the evidence presented, there could be no violation of the *Erie* doctrine on the grounds asserted by petitioner.

CONCLUSION

Petitioner has failed to support its contention that this case presents sufficiently important questions which warrant the review of this Court. Upon close examination it is clear that petitioner's claim that the Court of Appeals misapplied *Neely* v. *Martin K. Eby Construction Co..*, 386 U.S. 317 (1967) is illusory. Furthermore, it is equally apparent that the Court of Appeals fully complied with the decision of this Court in *Erie Railroad Co.* v. *Tompkins*, 304 U.S. 64 (1938) when it entered final judgment in favor of the respondent on the issue of conversion. Indeed, the relief sought by petitioner in this Petition for Certiorari would result in and not prevent a violation of both *Neely* and *Erie*. Therefore, respondent respectfully moves this Court to deny the Petition for Certiorari.

Respectfully submitted,

S. D. ROBERTS MOORE
W. CHARLES WADDELL, III
GUY M. HARBERT, III
GENTRY, LOCKE, RAKES & MOORE
P.O. Box 1018
Roanoke, VA 24005
Attorneys for Respondent

Of Counsel
HOWARD C. MCELROY
WHITE, ELLIOTT & BUNDY
P.O. Box 500
Abingdon, VA 24210

No. 86-1087

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

A & E SUPPLY COMPANY, INC.,
Petitioner,

v.

NATIONWIDE MUTUAL FIRE INSURANCE COMPANY,
Respondent.

Reply To Brief In Opposition To Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Fourth Circuit

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THOMAS R. SCOTT, JR.
E.K. STREET
STREET, STREET, STREET, SCOTT
& BOWMAN
P.O. Box 2100
Grundy, VA 24614
(703) 935-2128
Attorneys for Petitioner

Of Counsel:
STEPHEN A. SALTZBURG
Professor of Law
University of Virginia
School of Law
Charlottesville, VA 22901

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SUMMARY OF THE ARGUMENT

This case presents a simplistic setting in which the court of appeals reversed an ambiguous jury verdict in favor of petitioner for punitive damages on the tort of conversion, contrary to state law, and denied petitioner a jury trial on its slander claim that the trial judge declared had been erroneously dismissed in his post-trial opinion. Respondent endeavors to portray the facts in a complex light and the issues as seemingly unimportant in an effort to dissuade this Court from addressing the significant questions of federal law having an obvious impact on federal--state relations.

Respondent totally ignores the most significant point raised in the Petition for Certiorari: The trial court expressly declared that it committed error in denying

petitioner the opportunity to include its slander claim in the amended complaint prior to trial. 612 F. Supp., 760, 762, n. 1 (W.D. Va. 1985). Although the trial court recognized its error in the post-trial opinion, it had no way of correcting it since petitioner prevailed on the jury verdict. Petitioner, unlike respondent, had nothing to appeal to the court of appeals. The slander claim did not become crucial until the court of appeals reversed the trial court's judgment on the other tort claims. When the court of appeals declined to remand the case to the trial court on rehearing, it deprived petitioner of its right to trial by jury on the slander claim, which respondent concedes would support a verdict for punitive damages regardless of whether compensatory or nominal damages are awarded. (Brief in Opposition, at 13.)

Respondent urges that the court of appeals properly exercised discretion in denying petitioner an opportunity to be heard on its slander claim. In doing so, respondent disregards the fact that the slander claim has never been litigated since it was not appealable in the first instance and that the court of appeals declined to remand it on rehearing after reversing the trial court's judgment in the original appeal. There is nothing in the Federal Rules of Civil Procedure or the decisions of this Court that suggests, let alone supports, such a result.

Respondent also fails to recognize that the jury did find compensatory or nominal damages for conversion under the trial court's charge. The jury simply did not fix a specific amount. The cases relied upon by respondent in its Brief in Opposition actually support petitioner's contention that the court of appeals clearly erred in overturning the punitive damage verdict because the jury failed to determine any specific compensatory damage award. *See Zedd* v. *Jenkins*, 194 Va. 704, 708-09, 74 S.E.2d 791 (1953). As respondent concedes, nominal damages are sufficient to support a punitive damage award (Brief in Opposition, at 18), and they were found by the jury under the trial court's charge.

Finally, respondent concedes that under Virginia law a

state appellate court would remand a case for a new trial due to an ambiguity in a jury verdict when justice requires clarification, especially where the ambiguity was not caused by the verdict winner. (Brief in Opposition, at 17.) Under Fed. R. Civ. P. 51, the trial court instructed on actual and punitive damages that required the jury to determine whether petitioner was "entitled to be compensated for its damages" before punitive damages could be awarded. The trial court gave this instruction in connection with the tort theory urged by petitioner. Thus, any ambiguity in the instruction was the result of respondent's failure to object to language it believed correct when the trial judge instructed the jury.

Respondent urges for the first time on appeal that petitioner should have sought additional instructions directing the jury to actually award compensatory or nominal damages for conversion before awarding punitive damages. Respondent's contention is disingenuous and is intended to distract the Court's attention from the fact that the court of appeals, sitting in diversity, denied petitioner the right to a new trial to clarify an ambiguity in the verdict recognized in state courts under Virginia law.

ARGUMENT

A. The Petitioner Could Not Cross-Appeal Its Slander Claim Which The Trial Court Held Had Been Mistakenly Taken Away From The Jury Prior To Trial.

The following facts are undisputed: First, the trial court dismissed petitioner's slander claim prior to trial as improperly pleaded in the amended complaint. 612 F. Supp. at 762, n. 1. Second, the slander claim was not separately tried before the jury along with the other tort claims, but undisputed evidence of slander was proven under general allegations of bad faith. *Id.* Third, the trial court reconsidered its ruling in its post-trial opinion and held that the slander claim should have been permitted to proceed,

although a new trial was not ordered since petitioner obtained all relief requested under the remaining tort claims. *Id.* Fourth, under Virginia law, imputation of crime, i.e., arson, constitutes slander per se and actual damages need not be proved or awarded to sustain a verdict for punitive damages. *Newspaper Publishing Corp.* v. *Burke,* 216 Va., 800, 805, 224 S.E.2d 132, 136 (1976). Fifth, the court of appeals refused to remand the slander claim to the trial court for a new trial notwithstanding its characterization of respondent's actions as *"discreditable,"* 798 F.2d 669, 672 (4th Cir. 1986), and its finding that respondent *"did not relay its unfounded suspicions [of arson] to law enforcement authorities for proper investigation . . . and told creditors [of petitioner] that [it] had burned the building to collect on [the] insurance policy."* *Id.* at 670. (Emphasis supplied.) Sixth, the court of appeals gave no reason for its ruling. (Petition for Certiorari, at App. 20a.)

On these facts, there is no question that petitioner could not cross-appeal the trial court's post-trial holding that it committed error by dismissing the slander count in the amended complaint. *See New York Telephone* v. *Maltbie,* 291 U.S. 645, 646 (1934). In effect, the trial judge held that he mistakenly denied petitioner the right to proceed on a legitimate cause of action, but found it unnecessary, and perhaps even impossible, to correct the error by way of a judgment since the jury awarded petitioner everything requested that it could have obtained on the slander claim.[1]

When the court of appeals reversed the punitive damage award on the conversion theory, it refused to give petitioner any opportunity for a new trial on its slander claim. Although the court of appeals' decision reversing the punitive damage award for conversion was incorrect (discussed *infra*), a new trial on the slander claim should have been awarded in any event. *See generally, Neely* v. *Eby*

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[1] Petitioner did cross-appeal the trial court's denial of other relief—i.e., the trial court's denial of attorney's fees and costs, its refusal to permit amendment of the ad damum seeking additional punitive damages, and its grant of judgment n.o.v. on the fraud count. But, petitioner had nothing to cross-appeal with respect to slander.

Construction Co., 386 U.S. 317 (1967).

Respondent erroneously relies upon several decisions of this Court in support of its contention that petitioner should have cross-appealed the dismissal of the slander claim. (Brief in Opposition, at 10-11.) These cases are inapposite for the reason previously stated in the Petition for Certiorari: *The trial court corrected its error in its post-trial opinion and petitioner was not seeking any relief under the slander theory that had not been awarded in the jury verdict on the other tort claims.* Under these circumstances, it is absolutely clear that petitioner could not cross-appeal on the slander claim. *New York Telephone* v. *Maltbie, supra.*

Unlike petitioner, respondent was entitled to appeal each adverse ruling of the trial court. Significantly, respondent did not appeal the trial court's ruling that it erred in dismissing the slander claim. Instead, respondent accepted the ruling and now contends that the court of appeals correctly refused to remand the slander claim that respondent implicitly admitted was valid by failing to appeal the trial court's decision.

Respondent's novel position can be reduced to the following proposition: *If a trial court dismisses a viable claim before trial and later confesses error in the dismissal, a court of appeals can reverse a judgment for the plaintiff below on another claim and refuse, without giving any reasons, to permit the plaintiff to return to the trial court to litigate the claim that was erroneously dismissed, even though the defendant below failed to challenge the trial court's determination that it should have permitted the dismissed claim to go to the jury.* Petitioner submits that this proposition is in direct conflict with *Neely, supra,* and this Court's concern for equitable treatment of verdict winners. *See Cone* v. *West Virginia Pulp & Paper Co.*, 330 U.S. 212, 217 (1947).

This court has not had the occasion to revisit *Neely* in twenty years. If the court of appeals' decision is left in tact, every verdict winner must henceforth cross-appeal or assert every hypothetical issue and ground for a new trial on appeal in his main brief. This would indeed be a radical departure from the principle established in *Neely* that a verdict winner can "choose for his own convenience when to make his case for a new trial" and that "he may . . .

seek rehearing from the court of appeals after his judgment has been reversed." 386 U.S. at 328-29.

B. The Court Of Appeals' Refusal To Remand The Slander Claim Denied Petitioner Its Right To Trial By Jury.

Petitioner observed in the Petition for Certiorari that the court of appeals ignored its right to a jury trial on the merits of the slander claim never reached by the trial court. *See Cone* v. *West Virginia Pulp & Paper Co., supra,* 330 U.S. at 217. The trial court found undisputed evidence of slander damaging to petitioner which "prevent[ed] the commencement of any new business and severely limit[ed] its ability to obtain credit." 612 F. Supp. at 762, n. 1. Respondent has never disputed this finding in either the court of appeals or this Court.[2] Yet, petitioner has been unable to secure a trial on the merits of its slander claim. The trial court found a trial unnecessary in light of the jury award and the court of appeals declined to remand without giving any reason for depriving petitioner of its Seventh Amendment right to trial by jury.

Unlike the plaintiff in *Neely,* who filed no petition for rehearing and failed to suggest any new trial grounds in her petition for certiorari, petitioner advised the court of appeals on rehearing that its slander claim had not been litigated due to the trial court's admitted error and inability to correct it since petitioner prevailed on the jury verdict. Petitioner cited authority clearly indicating that compensatory damages need not be proved under state law to

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[2] Respondent does suggest for the first time that the slander claim is barred by the statute of limitations (Brief in Opposition, at 11, n.5), even though the record does not reveal when the defamatory statements were made. Since the complaint was filed within several months of the loss after it was denied on the ground of arson, the slander claim in the amended complaint would not be time barred. *See* Fed. R. Civ. P. 15(c). In any event, respondent's contention is premature and should be addressed to the trial court after the slander claim is remanded.

support a punitive damage verdict for slander. *See, e.g., Newspaper Publishing Corp* v. *Burke, supra,* 216 Va. at 805. Petitioner complied with the procedure established by this Court in *Neely, supra,* 386 U.S. at 328-29, but the court of appeals both misapplied and ignored it. *See also, Weade* v. *Dichmann, Wright & Pugh, Inc.*, 337 U.S. 801, 808-09 & n. 8 (1949).

Respondent suggests that the court of appeals properly denied petitioner's request for a new trial on the slander claim in the exercise of its discretion under *Neely*. (Brief in Opposition, at 6.) However, the Seventh Amendment denies the court of appeals the power to simply brush away petitioner's slander claim by declining to remand it to the trial court. *Neely,* properly read, gives the court of appeals *discretion* to grant a new trial or to remand for consideration of a new trial motion when a verdict winner advances a new trial theory for the first time on appeal or rehearing. 386 U.S. at 328-29. It does not sanction denial of trial by jury on a claim properly raised and simply not reached by a trial court. Respondent's construction of *Neely,* at best, is strained and certainly does not withstand Seventh Amendment scrutiny.

C. The Court Of Appeals Refused To Give Petitioner A New Trial On Conversion That Would Have Been Given Under State Law.

Respondent recognizes that if a jury awards actual or nominal damages, it may return a verdict for punitive damages in tort. (Brief in Opposition, at 12-14.) In the instant case, the trial judge instructed the jury that if petitioner "is entitled to be compensated for its damages," then the jury "may also" award punitive damages. The jury obviously found that petitioner was entitled to compensatory or nominal damages for conversion under the trial court's charge and then awarded punitive damages. The jury did not specify the amount of actual or nominal damages because respondent did not ask for specification in the trial court's instruction. Under Fed. R. Civ. P. 51,

respondent was obliged to object to the trial court's charge to preserve this issue for appeal.

Respondent certainly understood that the trial court's instruction required the jury to find actual or nominal damages before punitive damages were awarded. Respondent did not ask the trial court to require the jury to return a specific sum because petitioner was satisfied with a finding of actual or nominal damages without any specific award. Any further instruction requiring the jury to return a specific award would have resulted in respondent's payment of additional damages beyond those actually found but not awarded under the instruction given. Once actual damages were found, the jury turned its attention to punitive damages.

Respondent agreed that the trial court's instruction was proper under Virginia law. However, the court of appeals itself resolved the abiguity in the verdict created by the absence of a specific award.[3] In doing so, the court of appeals denied petitioner the opportunity to have another jury resolve the ambiguity contrary to the Virginia Supreme Court's decision in *Zedd* v. *Jenkins, supra,* 194 Va. at 708, and this Court's decision in *Iacurci* v. *Lummus,* 387 U.S. 86 (1967). Both *Zedd* and *Iacurci* established many years ago that a plaintiff is entitled to remand due to an ambiguous jury verdict.

Respondent concedes that remand is required under *Zedd* where an ambiguity exists, but contends that the ambiguity in this case was somehow brought about by petitioner's failure to request a specific award for compensatory or nominal damages under its conversion claim. (Brief in

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[3] The court of appeals also suggested that compensatory or nominal damages in tort were not independent of the damages underlying the contract breach. 798 F.2d at 673. *But see Jefferson Coals* v. *Eagle Energy,* Record no. 860031 (Va. S. Ct., App. awarded July 28, 1986) (suggesting that state trial court erred, and district court, in present case, ruled correctly that tort compensatory damages need not be proved in addition to those underlying contract breach to support punitive damage award, 612 F. Supp. at 766-67); *see also* Petition for Certiorari at 6, n. 8.

Opposition, at 17.) Respondent suggests for the first time on appeal that an additional instruction should have been given directing the jury to award actual or nominal damages. But, Fed. R. Civ. P. 51 imposed on respondent the obligation to request an additional instruction if it believed that the one given was not adequate. Surely, this Court will not countenance a verdict loser's complaints about an instruction raised for the first time on appeal at the expense of a verdict winner who could not respond to something never advanced at trial.

The Virginia Supreme Court, like most courts, is empowered to "render final judgment upon the merits" and to remand for a new trial "when the ends of justice require it." 2 Va. Code § 8.01-681 (1984). The Virginia Supreme Court has most recently examined the statutory scope of appellate review in *Erie Ins. Exch.* v. *Meeks,* 223 Va. 287, 291, 288 S.E.2d 454, 457 (1982), reprinted herein at Appendix 1a.

In *Meeks,* the plaintiff, brought suit on a judgment against her tort-feasor's liability insurer. The insurer denied liability contending that its insured breached the "notice" and "suit-papers" provisions of the policy. The trial court held that the insurer had the burden to prove lack of cooperation and prejudice under the state insurance code, and the plaintiff, therefore, offered no evidence that the insured complied with the provisions of the policy.

On appeal, the insurer contended that the plaintiff failed to make out a *prima facie* case due to the deficiency in the evidence and that the court should reverse and dismiss the action rather than remand it. The Virginia Supreme Court observed that "as a practical matter, once the trial court made its ruling on burden of proof and announced its interpretation of the [state insurance code], proof that [the insured] had performed the conditions precedent to recovery under his policy became superfluous." 223 Va. at 291. The Supreme Court accordingly held that "the ends of justice require a new trial." *Id.*

Had the instant case been tried in state court where it was originally filed, the Virginia Supreme Court may have

reversed the punitive damage award in the absence of a specific award for compensatory or nominal damages in tort. *But see* n.3, *supra.* However, it certainly would have remanded the case for a new trial in the *"interests of justice"* due to the ambiguity in the verdict and the trial court's ruling. *Id.; Zedd,* 194 Va. at 707-08; *Meeks,* 223 Va. at 291. In short, remand is completely consistent with this Court's holding in *Neely* that litigation should not be terminated when circumstances exist analogous to those in this case. *See* 386 U.S. at 327.

CONCLUSION

Petitioner respectfully asks this Court to grant the Petition and to reverse the decision of the Court of Appeals for the reasons stated herein and those previously assigned in the Petition for Certiorari.

Respectfully submitted,
THOMAS R. SCOTT, JR.
E.K. STREET
STREET, STREET, STREET, SCOTT & BOWMAN
P.O. Box 2100
Grundy, VA 24614
(703) 935-2128
Attorneys for Petitioner

Of Counsel:
STEPHEN A. SALTZBURG
Professor of Law
University of Virginia
School of Law
Charlottesville, VA 22901

APPENDIX

Erie Ins. Exch. v. Meeks, 223 Va. 287.

Syllabus.

Richmond

ERIE INSURANCE EXCHANGE

V.

DORIS PAULINE MEEKS

March 12, 1982.

Record No. 791278.

Appeal from a judgment of the Circuit Court of Louisa County. Hon. Harold H. Purcell, judge presiding.

Reversed and remanded.

Russell H. Roberts (Roberts, Crosley, Haley & Ashby, on brief), for appellant.

Buford M. Parson, Jr. (Patrick J. Nooney; W. W. Whitlock; May, Miller and Parsons, on brief), for appellee.

POFF, J., delivered the opinion of the Court.

In February, 1976, Doris P. Meeks was injured when rocks thrown by the wheels of a car operated by Robert A. Foley broke the windshield of the car in which she was riding. Foley did not stop, and Meeks followed him to his place of employment. Foley gave her a fictitious name, asked her not to report the incident, and assured her that he would have his insurance company contact her. Upon Meek's complaint, Foley was convicted of reckless driving.

In February 1977, papers in a tort action filed by Meeks were served on Foley. Government Employees Insurance Company (GEICO), Meek's uninsured motorists carrier, filed an answer, and trial was set for May 5, 1977. Pre-trial

depositions disclosed that Foley had a standard automobile liability insurance policy with Erie Insurance Exchange (Erie) on the day of the accident. On April 22, 1977, GEICO notified Erie of the accident, the pending tort action, and the date fixed for trial and mailed Erie copies of the suit papers.

On May 2, 1977, GEICO settled Meek's claim and its counsel withdrew from the case. Erie refused an offer of continuance and declined to defend the tort action, and the trial court entered a default judgment against Foley in the sum of $30,000.

Meeks then brought an action against Erie to enforce Foley's contractual rights. Meeks alleged that Erie "has wrongfully denied coverage to Robert A. Foley" and that Meek's tort judgment "remains outstanding and is the obligation of [Erie] to satisfy under the terms of the aforesaid policy". In its grounds of defense, Erie admitted that Foley's policy was in effect on the date of the accident but denied liability.

Adopting Meek's argument, the trial court ruled that, in light of Erie's admission, Meeks was not required to prove the terms of the contract; that Erie bore the burden of proving, as an affirmative defense, that Foley had failed to comply with the terms of the policy; and that Erie should present its evidence first. Erie objected to the ruling and offered a motion to strike. The motion was overruled, and Erie introduced the policy as an exhibit. The policy required Foley to give Erie "written notice" of an accident "as soon as practicable" and to "immediately forward" papers in any claim or suit filed against him. Erie called two witnesses who testified that Foley had never notified Erie of the accident or forwarded the papers in the tort action and that Erie had not learned what had happened until contacted by GEICO more than a year after the accident.

[1] At the conclusion of Erie's evidence, Erie renewed its motion to strike because Meeks had presented no evidence. The trial court overruled the motion. Meeks moved to strike Erie's evidence on the ground Erie had failed to prove prejudice. Meeks argued that Code § 38.1-381 as amended in 1966 requires an insurer to prove prejudice in order to deny coverage for breach of the notice

and suit-papers provisions of an automobile liability insurance policy. The trial court agreed, sustained the motion, and, by order entered June 14, 1979, granted Meeks summary judgment in the amount of the judgment Meeks had acquired in the tort action.

The first question we consider is whether the trial court erred in its construction and application of the 1966 amendment. As Meeks acknowledged in oral argument, this question is controlled by our decision in *State Farm* v. *Porter,* 221 Va. 592, 272 S.E.2d 196 (1980). There, we were asked to construe the 1966 amendment which, in effect, requires an insurer to prove prejudice before it has the right to deny coverage because of an insured's "failure or refusal . . . to cooperate with the insurer under the terms of the policy". Acts 1966, c. 182.[1]. We held that the General Assembly intended this amendment to apply only to the "cooperation" clause of the policy[2] and that "[t]he giving of notice of the accident, the giving of notice of suit, and the forwarding of suit papers were conditions precedent to coverage under the policy, requiring substantial compliance by the insured." 221 Va. at 599, 272 S.E.2d at 200; *accord, Liberty Mutual Ins. Co.* v. *Safeco,* 223 Va. 317, 288 S.E.2d 469 (1982).

Meeks urges us to "reconsider" this decision. We have done so, and, reaffirming our reasoning there, we hold that the trial court erred in its construction and application of the 1966 amendment.

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[1] Under this Act, Code § 38.1-381(al) read in pertinent part as follows: (al) Nor shall any such policy . . . be so issued . . . unless it contains an endorsement or provision insuring the named insured and any other person responsible for the use of . . . the motor vehicle . . . notwithstanding the failure or refusal of the named insured or such other person to cooperate with the insurer under the terms of the policy; provided, however, that if such failure or refusal prejudices the insurer in the defense of an action for damages arising from the operation or use of such motor vehicle, then this endorsement or provision shall be void.

[2] An amendment with similar effect, not applicable to *Porter* or the instant case, was addressed to the suit-papers provision by Acts 1980, c. 331.

[2] We now consider the trial court's ruling that Erie had to bear the original burden of proof. As we noted in *Porter,* we had held in several cases (all decided before the instant case was tried) that "performance" by the insured of the obligations imposed by the policy is "a condition precedent to recovery under the policy." *Id.* at 597, 272 S.E.2d at 199. As the trial court observed, Erie asserted an affirmative defense. With respect to such a defense, a defendant bears the ultimate burden of persuasion and assumes the risk of non-persuasion.

However, Erie did not bear the *initial* burden of going forward with the evidence as the trial court ruled. It is elemental that a plaintiff must prove a *prima facie* case. In her action to enforce Foley's rights under his contract, Meeks stood in Foley's shoes. In that posture, she alleged that Erie had "wrongfully denied coverage" and, thus, was in breach of the covenant to pay the tort judgment against Foley. It was Meek's burden to introduce evidence to support those allegations. Only after she had made a *prima facie* case that Foley had performed the conditions precedent to recovery would the burden of persuasion have fallen upon Erie. Accordingly, we hold that the trial court erred in its ruling.

[3] For the errors committed below, we will reverse the judgment in this case. Meeks argues that, since the judgment was entered before we issued our mandate in *Porter,* this case should be remanded for a new trial to afford her an opportunity to prove that Foley substantially performed the notice and suit-papers requirements of his policy.

When we reverse an erroneous judgment, we are empowered to "render final judgment upon the merits whenever, in the opinion of the court, the facts before it are such as to enable the Court to attain the ends of justice", and "[a] civil case shall not be remanded for a trial de novo except when the ends of justice require it". Code § 8.01-681. Construing a predecessor statute, we reversed and entered final judgment when we found, "no reason to believe that, upon another trial, any new or different evidence might be introduced which ought to affect the result." *A.C.L.R. Co.* v. *Walkup Co.,* 132 Va. 386, 395, 112 S.E. 663, 666 (1922). *See also Virginia Iron, Etc. Co.* v. *Odle's*

Adm'r, 128 Va. 280, 310-11, 105 S.E. 107, 117 (1920).

As a practical matter, once the trial court made its ruling on burden of proof and announced its interpretation of the 1966 amendment, proof that Foley had performed the conditions precedent to recovery under his policy became superfluous. Meeks had subpoenaed Foley as a witness at trial. In opening statement, Meek's counsel had told the jury that Foley would testify and that his testimony would supply such proof. Accordingly, we have reason to believe that, upon another trial, Foley's testimony might be introduced and, if believed, could affect a jury's verdict in this case. Hence, we are of opinion the ends of justice require a new trial.

The judgment will be reversed and the case remanded for a new trial, limited to the question whether Foley substantially performed the notice and suit-papers requirements of his policy. *See Glens Falls Indemnity Co.* v. *Harris,* 168 Va. 438, 191 S.E. 644 (1937) (insured's judgment reversed, case remanded, new trial limited to question of timely notice of injury).

Reversed and remanded.